No. 87-1101-ASX
Status: GRANTED

Title: GTE Sprint Communications Corporation, Appellant
v.
Roger D. Sweet, etc., et al.

Docketed:
December 31, 1987

Court: Supreme Court of Illinois

Counsel for appellant: DiGiantonio, Laura

Vide:
87-826

Counsel for appellee: Moritz, Terry F.

Entry	Date	Note	Proceedings and Orders
1	Dec 31 1987	G	Statement as to jurisdiction filed.
3	Jan 11 1988		Order extending time to file response to jurisdictional statement until January 29, 1988.
4	Jan 29 1988		Motion of appellees Illinois Dept. of Revenue, et al. to affirm filed. VIDED.
5	Feb 3 1988		DISTRIBUTED. February 19, 1988
6	Feb 9 1988	X	Reply brief of appellant GTE Sprint Communications Corp. filed.
7	Feb 22 1988		PROBABLE JURISDICTION NOTED. The case is consolidated with 87-826, and a total of one hour is allotted for oral argument. **
9	Mar 7 1988		Order extending time to file brief of appellant on the merits until April 29, 1988.
10	Apr 28 1988		Brief amicus curiae of National Taxpayers Union filed. VIDED.
11	Apr 29 1988		Joint appendix filed. VIDED.
12	Apr 29 1988		Brief of appellants Jerome F. Goldberg, et al. filed. VIDED.
13	Apr 29 1988		Brief of appellant GTE Sprint Communications Corp. filed. VIDED.
14	May 13 1988	D	Motion of appellant GTE Sprint Communications Corporation for divided argument filed.
15	May 20 1988		Order further extending time to file brief of appellee on the merits until June 15, 1988.
16	May 31 1988		Motion of appellant GTE Sprint Communications Corporation for divided argument DENIED.
17	Jun 9 1988		Order further extending time to file brief of appellee on the merits until June 22, 1988.
18	Jun 22 1988		Brief amici curiae of National Conference of State Legislatures, et al. filed. VIDED.
19	Jun 22 1988		Brief of appellees Illinois Department of Revenue, et al. filed. VIDED.
20	Jun 22 1988	G	Motion of MCI Telecommunications Corporation for leave to file a brief as amicus curiae filed.
21	Jul 6 1988		CIRCULATED.
22	Jul 11 1988	G	Application (A88-31) for an extension of time within which to file a reply brief, submitted to Justice Stevens.
27	Jul 13 1988		Application (A88-31) granted by Justice Stevens extending the time to file until August 5, 1988.
28	Jul 15 1988		Set for argument. Wednesday, October 12, 1988. This case is consolidated with 87-1101. (2nd case) (1 hr.)
29	Aug 5 1988	X	Reply brief of appellants Goldberg & McTigue filed. VIDED.
30	Aug 5 1988	X	Reply brief of appellant GTE Sprint Communications Corp. filed. VIDED.
31	Sep 15 1988		Motion of MCI Telecommunications Corporation for leave to file a brief as amicus curiae GRANTED.
32	Oct 12 1988		ARGUED.

87-1101 (1)

No.

In The Supreme Court of the United States

October Term, 1987

GTE SPRINT COMMUNICATIONS CORPORATION,

Appellant,

v.

ROGER D. SWEET, Director of the Illinois Department of Revenue, and JEROME COSENTINO, Treasurer of the State of Illinois,

Appellees.

On Appeal from the Supreme Court of Illinois

JURISDICTIONAL STATEMENT

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QUESTION PRESENTED

The Illinois Telecommunications Excise Tax Act imposes a tax on "the privilege of originating or receiving" long distance telephone calls in Illinois. This tax places a 5% assessment on the gross charge for long distance calls which either begin or end in Illinois and which are charged to an Illinois service address, but regardless of where such charges are billed or paid for.

The Illinois statute, acknowledging that other states may likewise seek to tax the long distance calls taxed by Illinois, provides that any taxpayer who pays tax both to Illinois and another state on the same long distance call may obtain an Illinois tax credit. The credit provided by Illinois is not in the amount of the Illinois tax, but is calculated by the amount of the tax the taxpayer has paid to the state other than Illinois. Obtaining this credit is contingent upon the taxpayer proving that the other state tax has been imposed on the same event taxed by Illinois, and that the other tax is "properly due" and has been paid for in the other state. The statute provides no criteria for determining whether another state's tax covers the same activity covered by the Illinois tax, or for determining when a tax in another state is "properly due."

The Illinois tax also places a 5% assessment on the gross charge for calls which occur entirely within the State of Illinois.

The question presented on this appeal is whether the Illinois tax, as applied to interstate long distance telephone calls as described above, violates the Commerce Clause of the Constitution of the United States.

PARTIES TO THE PROCEEDINGS

The parties to the trial proceeding below were as follows: Jerome F. Goldberg and Robert McTigue were original plaintiffs in this suit. J. Thomas Johnson, Director of Revenue for the Department of Revenue of the State of Illinois, was the original defendant below. (Roger D. Sweet has succeeded Johnson as Illinois Director of Revenue and has been substituted herein, pursuant to United States Supreme Court Rule 40.) The following long distance telephone carriers were originally named as nominal defendants: GTE Sprint Communications Corporation, SBS Skyline, Western Union, Max Long Distance, TDX Systems, Inc., MCI Telecommunications Corp., ITT, Allnet Dial 1 Service, Republic Telecom Corporation, U.S. Telecom, AT&T, Electronic Office Centers of America, Inc., and Illinois Bell Telephone. GTE Sprint Communications Corporation ("GTE Sprint"), one of the nominal defendants below, filed a cross-claim against the Illinois Director of Revenue (adding James H. Donnewald, Treasurer of the State of Illinois, as a defendant as well), challenging the validity of the Illinois tax at issue. (Jerome Cosentino has since become Treasurer of the State of Illinois and has been substituted herein, pursuant to United States Supreme Court Rule 40.)

J. Thomas Johnson and James Donnewald took a direct appeal from the trial court to the Illinois Supreme Court. Goldberg, McTigue and GTE Sprint were appellees on that appeal. None of the original nominal defendants below, other than GTE Sprint, participated in the appeal and they have therefore not been named herein as parties.

Goldberg and McTigue subsequently appealed from the judgment of the Illinois Supreme Court, filing a Jurisdictional Statement with this Court on November 20, 1987. GTE Sprint is also appealing from that judgment of the Illinois Supreme Court, and now submits this Jurisdictional Statement pursuant thereto.

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JURISDICTIONAL STATEMENT

GTE Sprint Communications Corporation appeals from the final judgment of the Supreme Court of Illinois, dated June 24, 1987 (with opinion filed July 27, 1987), holding the Illinois Telecommunications Excise Tax Act constitutional under the Commerce Clause of the Constitution of the United States.[1]

OPINIONS BELOW

The opinion of the Illinois Supreme Court is reported at 117 Ill. 2d 493, 512 N.E.2d 1262 and is reprinted in Appendix C to the Jurisdictional Statement already filed in this Court by plaintiffs and appellees below, Jerome F. Goldberg and Robert McTigue. *See Jerome F. Goldberg and Robert McTigue v. Roger D. Sweet, et al.*, No. 87-826 (docketed in the United States Supreme Court Nov. 20, 1987).[2]

The findings and opinion of the Circuit Court of Cook County, Illinois, dated October 22, 1986, are not reported. A copy of the trial court's findings of fact and conclusions of law are included in Goldberg App. E at 18a-24a.

JURISDICTION

This is an appeal from a judgment of the Illinois Supreme Court, holding the Illinois Telecommunications Excise Tax Act ("Tax Act" or "Act") constitutional. This judgment was entered on June 24, 1987. A written opinion supporting this judgment was filed on July 27, 1987.

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[1] The parent company of GTE Sprint Communications Corporation is GTE Communications Services, Inc., a Delaware corporation. GTE Sprint has no subsidiaries (other than wholly-owned subsidiaries) nor any affiliates of its own.

[2] The Goldberg/McTigue Jurisdictional Statement has been filed in order to appeal from the same Illinois Supreme Court judgment from which GTE Sprint now appeals. The Appendices attached to the Goldberg Jurisdictional Statement shall therefore be relied upon herein and referred to as "Goldberg App."

Between the issuance of the June 24 order and the July 27 opinion, GTE Sprint filed a timely petition for rehearing with the Illinois Supreme Court. The Illinois Supreme Court thereafter denied GTE Sprint's Petition for Rehearing, by order of October 5, 1987. A copy of the court's denial is included in the Appendices hereto (hereafter "Sprint App."). Sprint App. B at 6a. GTE Sprint subsequently filed its Notice of Appeal from the June 24 judgment with the Illinois Supreme Court, on December 8, 1987. Sprint App. A at 1a. GTE Sprint now submits its Jurisdictional Statement, within 90 days of the denial of its Petition for Rehearing, in order to appeal the judgment of the Illinois Supreme Court. The jurisdiction of this Court is invoked under 28 U.S.C. § 1257(2) (1982).

CONSTITUTIONAL AND STATUTORY PROVISIONS

Commerce Clause, United States Constitution: "The Congress shall have Power . . . to regulate Commerce with foreign Nations, and among the several States. . . . " Art. I, § 8, cl. 3.

The full text of the Illinois Telecommunications Excise Tax Act, Ill. Rev. Stat. ch. 120, §§ 2001-2021 (1985) is set forth in Goldberg App. F at 25a-47a.

The relevant text of several state taxing statutes and municipal ordinances, not directly at issue but referred to herein, are included as Sprint Appendices D through H at 11a-22a.

HOW THE FEDERAL QUESTION WAS RAISED

Jerome F. Goldberg and Robert McTigue, as plaintiffs below, raised the claim that the Illinois Telecommunications Excise Tax Act violated the Commerce Clause of the United States Constitution, as well as certain provisions of the Illinois constitution. Nominal defendant GTE Sprint, in a cross-claim against the State of Illinois, likewise asserted that the Tax Act violated the Commerce Clause.

The State of Illinois subsequently filed a motion for summary judgment, requesting that the court find the Tax Act constitutional under both the federal and Illinois constitutions. Goldberg/McTigue and GTE Sprint then filed cross-motions for summary judgment, GTE Sprint requesting partial summary judgment on the Commerce Clause ground alone. In its findings and conclusions on the cross-motions for summary judgment, the trial court stated that the "Illinois [Tax] Act violates the commerce clause of the [United States] Constitution," granting GTE Sprint's motion. Goldberg App. E at 22a and 24a.

The State of Illinois then appealed this decision directly to the Illinois Supreme Court, as provided by Illinois law. In an order entered June 24, 1987 and subsequent opinion filed July 27, 1987, the Illinois Supreme Court found the Tax Act valid, specifically holding that "the [Illinois] tax is valid under the commerce clause." Goldberg App. C at 14a; Goldberg App. D at 17a. The Illinois Supreme Court thus considered and expressly rejected GTE Sprint's federal claim.

STATEMENT OF THE CASE

A. GTE Sprint's Interstate Business and Operations [3]

GTE Sprint Communications Corporation is a retailer of intrastate and interstate telecommunications services. Sprint App. C at 7a. A large portion of GTE Sprint's business consists of providing paying customers interstate voice transmission services, by telephone, in all fifty states of the United States and in several foreign countries. Sprint App. C at 7a. In order to provide these services, GTE Sprint has established, over the years and at great expense, its own

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[3] An affidavit submitted by GTE Sprint in the trial court, detailing certain aspects of its operations, has never been challenged by the State of Illinois and has been attached to the Appendices hereto as part of the record necessary for an understanding of this appeal. Sprint App. C at 7a-10a.

interstate transmission network comprised of microwave radio, fiber optic, satellite and cable facilities, spread over numerous states. Sprint App. C at 7a-8a.

In transmitting voice messages on an interstate basis, GTE Sprint utilizes its own transmission facilities where possible. However, GTE Sprint must also purchase the services of other telecommunications carriers to complete its transmissions in certain areas its network does not reach. Sprint App. C at 8a.

The total costs GTE Sprint incurs in sending its interstate transmissions stem from several sources — from the costs of building and maintaining its interstate lines, the costs of sending transmissions over its interstate lines, the cost of purchasing the use of other carriers' lines in numerous other states where Sprint has not built lines, and the cost of access charges which must be paid to other carriers to pick up and drop off calls at the local level. Sprint App. C at 8a–9a. These are costs which GTE Sprint incurs in sending each interstate transmission and which emanate from activities occurring in each of the states involved in the path of the interstate transmission. Sprint App. C at 8a–9a.

These costs of interstate transmission are recovered by GTE Sprint from its customers in the tariffed prices the customers pay for telecommunications services. The customer's charge for an interstate toll call varies according to duration of the call and the distance between the place the call originates and the place it terminates; the call increases in price both as the duration of the call and the distance between these points increases. The transmission costs to GTE Sprint on long distance calls also increase the further it must transmit each such call. Sprint App. C at 9a.

GTE Sprint is capable, from an administrative viewpoint, of billing more than one state's tax on a single interstate communication. For example, GTE Sprint, in billing

to an Illinois address for an interstate transmission originating in Illinois and terminating in New York, could include in the charge for that call not only a tax assessed by Illinois, the originating state, but also a tax assessed by New York, the terminating state, as well as any other tax assessed by any one of the other states on the call's transmission path. Sprint App. C at 9a.

GTE Sprint's intrastate telecommunications services are provided pursuant to tariffs authorized by the Illinois Commerce Commission, while its interstate telecommunications services are common carrier services subject to Federal Communications Commission regulation, under 47 U.S.C. §§ 153(e), 201 *et seq.* Sprint App. C at 9a.

B. The Illinois Telecommunications Excise Tax Act

Section 4 of the Illinois Telecommunications Excise Tax Act states:

> [A] tax is imposed upon the *act or privilege of originating in this State or receiving in this State interstate telecommunications* by a person in this State *at the rate of 5% of the gross charge* for such telecommunications purchased at retail from a retailer by such person.

Goldberg App. F at 29a, Ill. Rev. Stat. ch. 120, § 2004 (1985) (emphasis added). In a previous clause, "gross charge" is defined as "the amount paid for the act or privilege of originating or receiving telecommunications in this State. . . . " Goldberg App. F at 25a; Ill. Rev. Stat. ch. 120, § 2002(a) (1985). And "amount paid" is defined under the Act as "the amount charged to the taxpayer's service address in this State *regardless of where such amount is billed or paid.*" Goldberg App. F at 26a; Ill. Rev. Stat. ch. 120, § 2002(b) (1985) (emphasis added).

Section 4 of the Act contemplates that states other than Illinois will impose taxes on the same interstate calling activity taxed by Illinois and provides the following

credit provision for those situations:

> To prevent actual multi-state taxation of the act or privilege that is subject to taxation under this paragraph, any taxpayer, *upon proof* that that taxpayer has paid a tax in another state *on such event, shall be allowed a credit* against the tax imposed in this Section 4 *to the extent of the amount of such tax properly due and paid in such other state.*

Goldberg App. F at 29a-30a; Ill. Rev. Stat. ch. 120, § 2004 (1985) (emphasis added).

C. GTE Sprint Payments under the Tax Act

Under Section 5 of the Tax Act, the ultimate consumers of telecommunications services are held liable for the payment of the tax. However, a retailer of telecommunications services is held equally liable for the tax on the long distance call services it sells, whether or not that retailer has actually collected the tax. Goldberg App. F at 30a; Ill. Rev. Stat. ch. 120, § 2005 (1985).

From about September 15, 1985 to July, 1986, GTE Sprint paid to the State of Illinois approximately $2,600,000.00 in taxes allegedly due the State under the Illinois Telecommunications Excise Tax. At least $400,000.00 of this amount Sprint paid itself, rather than collecting it from its customers. Sprint App. C at 10a.

D. This Lawsuit

Plaintiffs Goldberg and McTigue filed this lawsuit against the State of Illinois on August 13, 1985, challenging the constitutionality of the Tax Act under the United States and Illinois constitutions. GTE Sprint was named as a nominal defendant in this suit, being a retailer responsible for collecting the tax. GTE Sprint filed a cross-claim against the State of Illinois, attacking the tax under the Commerce Clause of the United States Constitution. GTE Sprint simultaneously moved, under Illinois statute, to have the amounts it paid under the Tax Act placed into a protest fund, in order to preserve its right to a refund of its

payments if the Tax Act were ultimately declared unconstitutional. *See* Ill. Rev. Stat. ch. 127, § 172 (1985). The trial court granted GTE Sprint's motion and established a fund into which both GTE Sprint's and Sprint's customers' tax payments were and are being paid.

GTE Sprint subsequently filed a cross-motion for summary judgment on the validity of the tax under the Commerce Clause. The trial court, construing the tax as one on interstate calling activity, found that the Act failed to pass at least three of the four tests to be applied in a Commerce Clause challenge to a tax on interstate activity, as reflected in *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274 (1977). Goldberg App. E at 18a, 22a and 24a.

The State of Illinois appealed this decision directly to the Illinois Supreme Court, which reversed the trial court's decision. In doing so, the Illinois Supreme Court agreed with the trial court that the tax was assessed against interstate activity, and that, to survive constitutional muster, the tax must have sufficient nexus with the taxing state, must be apportioned to activity within the taxing state, must not discriminate against interstate commerce and must bear a fair relation to services provided by the taxing state, under *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274 (1977). Goldberg App. C at 9a, 10a and *passim*. Significantly, the court, in applying these tests, held that the Illinois tax failed two of them, *i.e.*, apportionment and discrimination. The court nevertheless upheld the tax by finding that the apportionment test is constitutionally dispensable and that the tax's discriminatory effect is "cured" by its tax credit provision. Goldberg App. C at 11a–13a. The Illinois Supreme Court thus concluded that the Illinois tax passed, in a fashion, the *Complete Auto* tests and "is [therefore] valid under the commerce clause." Goldberg App. C at 14a.

THE QUESTION PRESENTED IS SUBSTANTIAL

The question of whether Illinois may place a tax on gross charges for interstate calling activity poses a substantial constitutional question which should be addressed by this Court for several reasons. First, the issues presented by the imposition of the Illinois tax are novel ones; this Court has never scrutinized a tax such as the Illinois tax under Commerce Clause strictures. Second, precedent in the area of state taxation on interstate activities suffers from a general lack of clarity, so review of the question presented on this appeal is greatly needed to give states guidance. Third, the issue of the legality of state taxes on interstate phone communications is of enormous import, given the proliferation of such communications in recent years. *See* Jurisdictional Statement, *Goldberg v. Sweet*, No. 87–826 at 25, fn. 21. Finally, and most important, the lower court repeatedly erred in finding that the Illinois tax on long distance calls is constitutional under the Commerce Clause. As a consequence, compelling reasons exist for this Court not only to note probable jurisdiction on this appeal — but to reverse the judgment of the Illinois Supreme Court.

I. The Imposition of the Illinois Tax Violates the Commerce Clause

A. The Tax Is Applied to Interstate Activity

The imposition of any state tax on interstate activity raises the question of whether the tax contravenes limits on state interference with free trade set by the Commerce Clause of the United States Constitution. *American Trucking Associations, Inc. v. Scheiner*, 107 S. Ct. 2829, 2838–2839 (1987). If the Illinois Telecommunications Excise Tax Act is construed as applying to interstate activity, it follows, then, that a substantial Commerce Clause issue has been raised by the application of that tax.[4]

[4] GTE Sprint has standing to challenge the Illinois tax under

(Footnote continued on the following page)

The Illinois tax states that "a tax is imposed upon the *act or privilege of originating* in this State *or receiving* in this State *interstate telecommunications*." Goldberg App. F at 29a; Ill. Rev. Stat. ch. 120, § 2004 (1985) (emphasis added). Since interstate transmission is the very predicate and simultaneous necessity of 'originating or receiving' a long distance telephone call, the tax has clearly been laid on inherently interstate activity. Indeed, the Illinois Supreme Court (as did the trial court) acknowledged this fact by construing the taxable event under the Act as interstate activity. Goldberg App. C at 9a; Goldberg App. E at 20a–22a. Since this Court has traditionally deferred to state courts' construction of taxing statutes, there is every likelihood that this Court will conclude that the tax is applied to interstate activity, as well. *See, e.g., Memphis Natural Gas Co. v. Stone*, 335 U.S. 80, 84-85 (1948); *Coverdale v. Arkansas-Louisiana Pipe Line Co.*, 303 U.S. 604, 609 (1938).[5]

Further, it is unlikely that the State of Illinois' arguments below — that the tax is imposed on instate, as opposed to interstate, activity — will dissuade this Court from adopting the state courts' construction of the tax. For example, the State, ignoring the plain language of the statute, argued that, because the Tax Act is limited to long

4 *(continued)*

the Commerce Clause. *See* Statement of the Case, *supra* at 6-7; *Bacchus Imports, Ltd. v. Dias*, 468 U.S. 263, 267 (1984).

[5] It is also likely that this Court will construe the taxed activity as interstate in nature since the taxed activity has been so construed in other contexts. *See, e.g., Central Greyhound Lines, Inc. v. Mealey*, 334 U.S. 653, 661 (1948) (state's gross receipts tax on receipts from transportation which began and ended in New York but traversed other states was tax on "interstate commerce"); *Telegraph Co. v. Texas*, 105 U.S. 460, 465 (1881) ("occupation" tax on receipts of company sending telegraph messages across state lines was tax on interstate messages). Further, the communications taxed by Illinois are regulated by the F.C.C. as "interstate" activity. *See* Statement of the Case, *supra* at 5.

distance calls which are *charged* to a "service address" in Illinois, the tax is a local "sales" tax. But this characterization of the tax ignores the plain language of the statute which taxes the "privilege" of calling; it ignores the practical reality of the tax, which is to tax the calling activity, *Maryland v. Louisiana*, 451 U.S. 725, 756 (1981) (the "practical operation" of a tax controls in assessing its constitutionality); and, in any event, it ignores the fact that the tax cannot be deemed to tax a local "sales" transaction, as it explicitly taxes long distance calls even when they are *billed and/or are paid for outside Illinois*. Goldberg App. F at 25a–26a; Ill. Rev. Stat. ch. 120, § 2002(b) (1985). This Court will thus likely agree with the state courts and conclude that the tax applies to interstate activity.

B. The Tax Fails To Comply with Commerce Clause Requirements

If the Illinois tax is interpreted, as it should be, as a tax on interstate activity, substantial Commerce Clause issues come into play. *American Trucking Associations, Inc. v. Scheiner*, 107 S. Ct. 2829, 2832 (1987). The Commerce Clause of the United States Constitution has traditionally been interpreted by this Court as limiting the state's taxing power over interstate activity and requiring that such state taxes (a) be assessed only on that portion of the activity which occurs within the taxing state; (b) be assessed in such a way as not to discriminate against interstate commerce; and (c) be fairly related to services provided by the taxing state. *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977) ("*Complete Auto*"); *see also Maryland v. Louisiana*, 451 U.S. 725, 754 (1981). In applying these tests to the Illinois tax, serious questions arise as to the ability of the tax to meet any of these tests, both despite and in light of the Illinois Supreme Court decision finding the tax constitutional.

1. The Tax Is Not Apportioned

A tax on interstate activity, to meet Commerce Clause requirements, must be apportioned to that segment of the interstate activity which occurs within the taxing state. *Armco Inc. v. Hardesty*, 467 U.S. 638, 644 (1984); *Central Greyhound Lines, Inc. v. Mealey*, 334 U.S. 653, 662–63 (1948). The Illinois Supreme Court has already found that the Illinois tax utterly fails the apportionment test since it is not even vaguely limited to that portion of interstate calling activity which occurs in Illinois. As the court acknowledged, "[s]ince the instant tax applies to the entirety of [the gross charge for] each and every interstate telecommunication, it is not an apportioned tax." Goldberg App. C at 10a.

Applicable precedent confirms that the tax is unapportioned. For example, in *Central Greyhound Lines, Inc. v. Mealey*, 334 U.S. 653 (1948), New York passed a tax on the gross receipts from transportation which, though it originated and terminated in New York, was also routed through New Jersey and Pennsylvania. This Court nevertheless stated that the New York tax would be void under the Commerce Clause, unless it were apportioned, *i.e.*, limited to some percentage of the receipts equal to that percentage of the multi-state transportation which occurred in New York. The Illinois tax at issue here is the equivalent of that unapportioned New York gross receipts tax on interstate travel; just as the New York tax sought to tax gross charges for interstate transportation so, too, here Illinois seeks to tax gross charges for interstate communication. The Illinois tax, like the New York tax, does not limit itself to that portion of the charges which reflects that portion of the interstate activity occurring in the taxing

state.[6] Therefore, the Illinois tax fails the *Complete Auto* apportionment test.

A recent discussion of apportionment by this Court further underscores the apportionment deficiency of the Illinois tax. In *Container Corporation of America v. Franchise Tax Board*, 463 U.S. 159 (1983) (*"Container"*), the Court examined a corporate franchise tax applied to the income of businesses engaged in interstate activity. Being applied to income from interstate activity, the tax included an apportionment formula for determining that segment of income which could be attributed to—and therefore taxed by—the taxing state. The Court, in assessing the formula, held that, to be valid, the formula must have "external consistency," that is, the factors used in the formula to divide income attributable to instate activity, which is taxable, from income attributable to out-of-state activity, which is not taxable, "must actually reflect a reasonable sense of how income is generated." *Container*, 463 U.S. at 169.

It is obvious, however, that the Illinois tax fails this external consistency test. GTE Sprint submitted uncontested evidence below that the gross charge for an interstate call is generated not only by the use and cost of Illinois facilities but by the use and cost of significant out-of-state facilities as well. *See* Statement of the Case, *supra* at 4. But the Illinois tax is nevertheless assessed against the *entire* gross charge for a long distance call; there is no attempt to divide the gross charge, according to a realistic sense of how it is generated, between instate and out-of-state activity—and tax only that part which can be

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[6] The fact that Illinois only taxes charges charged to an Illinois service address does not apportion the tax. In *Central Greyhound* the New York tax was deemed objectionable even though the tax was limited to those receipts collected by the bus company in New York. *Central Greyhound Lines, Inc. v. Mealey*, 266 A.D. 648, 44 N.Y.S.2d 652, 654 (App. Div. 1943), *aff'd*, 696 N.Y. 18, 68 N.E.2d 855 (1946), *rev'd*, 334 U.S. 653 (1948).

said to be generated by Illinois activity or costs. As a consequence, the Illinois tax has no "external consistency," and is therefore unconstitutional under *Container*.[7]

As noted, the Illinois Supreme Court arrived at this same conclusion. However, the court did not strike down the tax on this basis. It reasoned, instead, that apportionment of a tax on interstate activity is simply not required if the tax otherwise avoids working discrimination against interstate commerce. But this Court, in *Complete Auto*, expressed the Commerce Clause tests to be applied to a tax on interstate activity in the conjunctive, so it appears that, contrary to the Illinois court's conclusion, the apportionment test cannot be so eliminated. *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977). In addition, this Court has elsewhere stated that the failure of a tax to apportion itself to instate activity portends, in itself, prohibited discrimination. *Armco Inc. v. Hardesty*, 467 U.S. 638, 644 (1984) ("A tax that unfairly apportions income from other States is a *form of discrimination* against interstate commerce." (emphasis added)).[8] As a result, the Illinois Supreme Court has erred. At the least, the Illinois

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[7] Although this Court, in *Moorman Manufacturing Co. v. Bair*, 437 U.S. 267 (1978), has held that a tax need not be perfectly apportioned, *Moorman* cannot support the validity of the Illinois tax because the Illinois tax has *no* apportionment formula. Compare, for example, a true apportionment formula, as contained in the current Florida tax on private line long distance calls, with the approach taken by the Illinois tax. The Florida tax is assessed only on a percentage of the charge for each interstate private line long distance call, determined according to that percentage of the total distance of the call which falls within Florida. The purpose of this apportionment is "to ensure that no more than 100% of the interstate charge can be taxed by this state and another state." Fla. Stat. Ann. § 212.005(e)2 (West 1987 General Laws Special Service); Sprint App. D at 11a-13a.

[8] In concluding that apportionment of a tax is not necessary if the tax is not "discriminatory," the Illinois Supreme Court relied

(Footnote continued on the following page)

Supreme Court's decision raises legal questions of constitutional significance which must be addressed—that is, whether the fair apportionment requirement of *Complete Auto* can be eliminated and, if it cannot, whether the Illinois tax on the gross charge for long distance calls can meet that requirement.

2. The Tax Discriminates against Interstate Commerce

Even if this Court were to conclude that the Illinois Supreme Court was correct in eliminating the apportionment test of *Complete Auto*, the application of the third *Complete Auto* test by the Illinois Supreme Court still raises substantial and novel constitutional issues. Under that test, a tax on interstate activity cannot operate so as to discriminate against interstate commerce. *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 287 (1977). GTE Sprint contended below that the tax failed this test because the tax effected discrimination against interstate commerce in two ways: First, the Illinois tax creates potential and actual taxation of the same interstate calling

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8 *(continued)*

on a Wisconsin state court case declaring a tax on interstate calling valid, *Wisconsin Telephone Co. v. Wisconsin Department of Revenue*, 125 Wis. 2d 339, 371 N.W.2d 825 (Ct. App. 1985), as well as on *Container Corp. of America v. Franchise Tax Board*, 463 U.S. 159 (1983) and *Japan Line Ltd. v. County of Los Angeles*, 441 U.S. 434 (1979). Goldberg App. C at 10a–11a. Not only is the Wisconsin case factually distinguishable from this case, but the Wisconsin court applied legal standards which have been categorically disapproved by this court in *Armco Inc. v. Hardesty*, 467 U.S. 638 (1984). *See* discussion *infra* at 20, fn. 12. Further, neither *Container* nor *Japan Line* supports the elimination of the apportionment requirement. Indeed, in both those cases, the Court states that a failure to apportion will most likely lead to discrimination. These statements are, in fact, virtual rebuttals of the Illinois court's contention that the apportionment requirement is expendable. *Container*, 463 U.S. at 170-71; *Japan Line*, 441 U.S. at 447.

activity by Illinois and other states, while purely intrastate calling activity is not exposed to such multiple burdens; and, second, although Illinois applies a 5% tax on both intrastate and interstate calls, this taxing scheme effectively taxes interstate calling more heavily than intrastate calling. The fact that the Illinois high court dismissed these two arguments, along with the manner in which it dismissed them, raises questions of substantial impact which this Court should address.

a. The Tax Discriminates by Imposing Multiple Burdens

Taxes which create even a risk of multiple taxation on the same interstate activity have traditionally been viewed as discriminatory and as imposing undue burdens on interstate commerce. *Western Live Stock v. Bureau of Revenue*, 303 U.S. 250, 255–56 (1938); *International Harvester Co. v. Department of Treasury*, 322 U.S. 340, 360 (1944)("the risk of multiple taxation creates the unconstitutional burden which actual taxation by [more than one state] would impose in fact"). This Court has recently reiterated and reinforced its position that a tax on interstate activity will be void if hypothetical, "like" taxes could be imposed by other states on the same activity. *Armco Inc. v. Hardesty*, 467 U.S. 638, 644–45 (1984) ("*Armco*"). *Accord Westinghouse Electric Corp. v. Tully*, 466 U.S. 388 (1984).

Applying the *Armco* holding here, it is clear that the Illinois tax should be invalidated. For example, Illinois assesses its tax on the total charge for the act or privilege of originating or receiving an interstate call in Illinois, if the call is charged to an Illinois service address. But Illinois taxes the call even if that call is billed or paid for in another state. *See* Statement of the Case, *supra* at 5. Suppose now a call from Illinois to New York. And suppose a New York tax *like* the Illinois tax—*i.e.*, one which covers calls originating or terminating in New York, where those calls are billed or paid for in New York. If a call is then

made from Illinois to New York, Illinois could tax the call because it begins in Illinois and could be charged to an Illinois address; but New York could also tax the call because the call terminates in the State of New York and the call, though charged to an Illinois address, might be either billed or paid for in New York.[9] Further, GTE Sprint has submitted uncontested facts which demonstrate that it could apply both the Illinois and New York tax, in this instance, to the same call. *See* Statement of the Case, *supra* at 4-5. *Ergo*, multiple taxation on the same charge for the very same call. Under *Armco*, the tax should therefore fall.

Even without relying on the *Armco* "hypothetical" test, however, it is clear that the Illinois tax is invalid since jurisdictions other than Illinois are already actually applying "like" taxes on the very calls taxed by Illinois. Although a showing of such instances of actual multiple taxation is not *necessary* to invalidate the Illinois tax, such a showing surely dooms it. *See American Trucking Associations, Inc. v. Scheiner*, 107 S. Ct. 2829, 2841 (1987).

And such a showing is easy to make. For example, taxes have been levied on interstate telecommunications services in other states, which, when combined with the Illinois tax, produce multiple taxation of the same activity. The City of Wheat Ridge, Colorado, a Denver suburb, has enacted an ordinance which applies a sales tax to "interstate and intrastate telecommunications service originating from or received on telecommunications equipment in this City if the charge for the service is billed to a person in this City or *billed to an affiliate or division of such person in any state/city on behalf of a person in this City.*" City of Wheat Ridge, Colorado Ordinance No. 630, § 2(b) (Aug. 12, 1985) (emphasis added); *see* Sprint App. E

[9] For example, a call might be *charged* to a phone at the Illinois division of a New York corporation, but the bill *paid* at corporate headquarters in New York.

at 14a-15a. Under this ordinance, a corporation headquartered in Chicago, with a branch office in Wheat Ridge, is subject to the Wheat Ridge tax on the gross charge for an interstate transmission between Wheat Ridge and Chicago, over GTE Sprint facilities, where the call is "billed" to Chicago corporate headquarters (an "affiliate"). But the charge for that call could also be taxed by Illinois because the call would have originated from or been received in Illinois and could also have been "charged" to an Illinois service address, *i.e.*, the Chicago corporate headquarters. The City of Greeley, Colorado has enacted an identical tax. Greeley City Ordinance No. 45, Sec. 1 (May 7, 1985); *see* Sprint App. F at 16a. There are other instances of other states' taxation of interstate calls originating or terminating in Illinois.[10]

The imposition of these taxes, together with the Illinois tax, can and do bring about multiple taxation of the same calling activity. Under the Illinois Act, Illinois has taxed the full stretch of an interstate transmission. But other states inevitably involved in the transmission of the same interstate call have equal right to assess taxes on

[10] Instances of actual multiple taxation result not only from other states' "sales" taxes. For example, Washington has passed a tax on the *privilege* of engaging in interstate phone calls. Wash. Rev. Code Ann. §§ 82.04.065 and 82.04.250 (1981 and Supp. 1987); Sprint App. G at 17a-19a. This tax is applied to the gross proceeds from all long distance calls originating or terminating in Washington state, where such calls are billed or paid for in Washington. As a consequence, a long distance call from Illinois to Washington and charged to an Illinois address, but paid for in Washington, could be taxed by both Illinois and Washington.

New Mexico also has a tax on the "privilege" of engaging in long distance phone calls. New Mexico places a tax on 65% of the gross receipts from calls originating or terminating in New Mexico. N.M. Stat. Ann. §§ 7-9-3, 7-9-4 and 7-9-56 (1986 and Supp. 1987); Sprint App. H at 20a-22a. This tax, in combination with the Illinois tax, results in multiple taxation of the same calls.

their own instate portion of it, whether that entails the origination or receipt of the call, the transmission of the call, or aspects of its sale (*e.g.*, "billing and payment"). As a consequence, the Illinois tax imposes an impermissible burden on interstate communications, not borne by instate ones.

The Illinois Supreme Court dismissed the problem of multiple taxation presented by the Illinois tax, adopting a highly convoluted approach. First, the court simply mischaracterized the tax in order to find that, with regard to communications which *originate* in Illinois, no risk of multiple taxation exists.[11] Goldberg App. C at 11a. But there is absolutely no evidence in the record—nor none cited by the court—which would support the court's conclusion that states other than Illinois could not tax calls originating in Illinois, or that the tax coverage differs between calls which originate and calls which terminate in Illinois. Indeed, to the contrary, GTE Sprint has submitted uncontested evidence here and below, in the form of actual taxes, establishing that other jurisdictions can, and do, tax calls taxed by Illinois, whether they begin or end in Illinois. *See* discussion *supra* at 16-17 and fn. 10. The court simply erred in concluding that calls originating in Illinois cannot be taxed by another state.

The Illinois Supreme Court further erred in its reliance on recent Wisconsin and Alaska state court cases

[11] The Illinois court construed the tax as covering those calls *originating* in Illinois which were "paid for in Illinois or billed to a service address located in Illinois," whereas it construed the tax as covering calls *received* in Illinois only when "billed to a service address in Illinois." Goldberg App. C at 11a. But, plainly, no such distinction exists in the Act. Calls, whether they originate or terminate in Illinois, are taxed under the Act when they are *charged* to an Illinois service address and, *in both instances*, regardless of where they are billed or paid for. Goldberg App. F at 25a-26a and 29a-30a; Statement of the Case, *supra* at 5.

upholding taxes on interstate telephone calls to support its position that calls originating in Illinois could not be subject to possible multiple taxation. *See* Goldberg App. C at 11a. Specifically, the Illinois court relied on the Alaska and Wisconsin courts' construction of their states' long distance phone call taxes as "sales" taxes and those courts' identical findings that those taxes were non-discriminatory because only one state could assess a tax on the "sale" of a long distance call, since the sale would invariably occur at a single location. *See Douglas v. Glacier State Telephone Co.*, 615 P.2d 580, 588 (Alaska 1980) ("*Douglas*"); *Wisconsin Telephone Co. v. Wisconsin Department of Revenue*, 125 Wis. 2d 339, 371 N.W.2d 825, 830 (Ct. App. 1985) ("*Wisconsin Telephone*"). But these state courts' conclusions cannot apply here, for three reasons.

First, the Illinois court has acknowledged that the Illinois tax is *not* a tax on a local sale, but a tax on the privilege of calling which is interstate—not local—in nature. Goldberg App. C at 8a-9a. Second, even if the Illinois tax were construed as a tax on the sale of services, that tax still carries a complication which prevents any conclusion that it avoids imposing a risk of multiple taxation. Specifically, the Illinois tax taxes interstate calls which begin or end in Illinois and which are charged to an Illinois service address, *regardless of where they are billed or paid for*. As a consequence, even if a call originates in Illinois, is charged there and is, therefore, taxed by Illinois, another state where the call terminates and where the call is paid for might also tax the call on the ground that the "sale" occurred there. Third, the Alaska and Wisconsin courts concluded that taxes such as the taxes under consideration there were not likely to be imposed by more than one state because they found that, practically speaking, a carrier could assess only one state's tax on any one long distance call, under the telephone system as it existed then in those states. *Douglas*, 615 P.2d at 588; *Wisconsin Telephone*, 371 N.W.2d at 830. But GTE Sprint has submit-

ted uncontested evidence which demonstrates, that, by contrast, the GTE Sprint system is not a system which functions in the manner the Bell system did in the *Douglas* and *Wisconsin* cases, and that it *can*, administratively, apply more than one state's tax to any interstate call. Sprint App. C at 9a. Thus, the Alaska and Wisconsin cases are no support whatsoever for the Illinois court's conclusion.[12]

Indeed, prior precedent which is pertinent points to the opposite conclusion—that the Illinois tax on long distance calls originating in Illinois *will* be deemed to impose the risk of multiple tax burdens on the same activity. For example, in *Michigan-Wisconsin Pipe Line Co. v. Calvert*, 347 U.S. 157 (1954) ("*Michigan-Wisconsin*"), Texas had imposed a tax on the "taking" of the full volume of gas into an interstate pipeline for interstate transmittal—that is, on the "origination" of the interstate flow. The court struck down the tax because, *inter alia*, it posed the risk of multiple taxation. The Court reasoned that, if Texas could place a tax on the origination of the interstate flow of gas, so, too, could the state where the interstate flow was terminated. *Michigan-Wisconsin*, 347 U.S. at 170. Likewise, here, if Illinois is permitted to apply a tax on the gross charge for an interstate call beginning in Illinois, so, too, must the state where the call terminates. As a consequence, the Illinois tax is unconstitutional under proper case authority, and the Wisconsin and Alaska state court cases, neither of

[12] In addition, both the Alaska and Wisconsin courts' legal reasoning has been rejected. Those courts upheld the taxes at issue because the plaintiffs had failed to demonstrate that the tax imposed *actual* multiple burdens. But, in *Armco Inc. v. Hardesty*, 467 U.S. 638 (1984), this Court categorically rejected this legal premise and held, instead, that *actual* multiple taxation need not be proven to invalidate a tax on interstate activity. The Wisconsin court also relied heavily on *General Motors Corp. v. Washington*, 377 U.S. 436 (1964) which has since been overturned in *Tyler Pipe Industries, Inc. v. Washington State Department of Revenue*, 107 S. Ct. 2810 (1987).

which was reviewed by this Court, do nothing to buttress the Illinois court's erroneous conclusion.

What is even more significant, however, is the fact that the Illinois Supreme Court simply conceded that, with regard to long distance calls that *end* in Illinois, jurisdictions other than Illinois currently *do* tax those same calls. Thus the court, after all its analytical gyrations designed to salvage the tax on calls which originate in Illinois, simply admits that the Illinois tax does impose actual multiple burdens with regard to calls that terminate in Illinois. Goldberg App. C at 12a–13a. This acknowledgment should lead to the inescapable conclusion that the tax is void. *Armco Inc. v. Hardesty*, 467 U.S. 638, 644-45 & n.8 (1984).

The Illinois Supreme Court managed to excuse this otherwise fatal flaw of the tax, however, by holding that the credit provision in the Tax Act "cures" its discriminatory effect. The Illinois credit provision allows a taxpayer who has paid Illinois and another state a tax on the same call activity, a tax credit from Illinois in the amount of the tax paid to that other state (or other states). But this credit mechanism is a totally illusory cure for multiple taxation. First, to obtain the credit, a taxpayer must prove each instance of multiple taxation. *See* Statement of the Case, *supra* at 5-6. Since the Illinois tax represents a tax on charges which are incurred with great frequency, such a proof procedure for each illegal taxing incident constitutes a significant burden in itself. This "cure," GTE Sprint maintains, is as bad as the disease, and increases, rather than decreases, the burdens on interstate commerce the tax imposes.

Second, the refund provision offers only sporadic elimination of prohibited multiple burdens. To illustrate: if State X imposes a tax on the gross charge for a call to Illinois at a rate of 3%, while Illinois imposes a tax on the gross charge for the same call as received in Illinois at

a rate of 5%, the fact that Illinois grants a credit in the amount of 3% of the charge does not negate the fact that the charge for the call is still being taxed by Illinois, without proper apportionment, albeit at a lower—2%—rate. It is only when the taxing state or states other than Illinois actually assess taxes in an amount which, alone or collectively, equals or exceeds the absolute amount of tax assessed by Illinois that the credit eradicates the Illinois tax and thereby eliminates its inherently discriminatory effect. The "cure" is thus totally fortuitous and cannot infallibly eradicate discriminatory taxation. *Halliburton Oil Well Cementing Co. v. Reily*, 373 U.S. 64, 76 (1963) (Brennan, J., concurring).

Third, the Illinois tax credit is provided only for taxes assessed by other states which are 'properly due,' and which cover the same activity covered by the Illinois tax. *See* Statement of the Case, *supra* at 5-6. But no clarification of what taxes are 'properly due' or what other taxes will overlap with the Illinois tax is provided by the taxing statute. This provision thus relegates to a taxpayer the burden of proving, in each instance of multiple taxation and without any criteria, that another state's tax is 'properly due,' and that another state's tax overlaps the Illinois tax, before the taxpayer can obtain a credit. Surely, placing this heavy burden on the taxpayer, in order to rectify the constitutional infirmities of a tax, constitutes, in itself, an undue burden on interstate commerce.[13]

The Illinois credit mechanism is totally inadequate to rescue the Illinois tax from its multiple burden infirmity. The Illinois court has conceded that the tax is unconstitutional without the credit mechanism. The tax must

[13] This Court has itself encountered significant difficulties in sorting out proper from improper state taxes on interstate activity, as well as in identifying 'taxable events.' *See* discussion *infra* at 27. What, then, must be the burden placed on the taxpayer?

fail, as a consequence. At the very least, GTE Sprint's position—whether the credit "cures" the discrimination—poses a significant issue for this Court which deserves plenary review.

b. The Tax Discriminates by Imposing Heavier Burdens on Interstate than on Intrastate Calls

The State of Illinois argued below that the Illinois tax could not be deemed "discriminatory," in any event, because the same or "equal" 5% tax was levied on both interstate and intrastate calls in Illinois. The gist of the argument, apparently, is that Illinois, having applied a 5% tax on instate calls, should also be permitted to impose a 5% tax on interstate calls; in this way, the interstate tax would simply constitute a tax which is "complementary" to the instate tax, just as a use tax is "complementary" to a sales tax. *Cf. Henneford v. Silas Mason Co.*, 300 U.S. 577 (1937). The Illinois Supreme Court apparently agreed. Goldberg App. C at 11a. However, that portion of the Illinois tax on interstate calls cannot be justified as a "compensatory" or "complementary" tax.

As this Court has stated, "[t]he concept of a compensatory tax first requires identification of the burden for which the state is attempting to compensate." *Maryland v. Louisiana*, 451 U.S. 725, 758 (1981). Here, the State must claim that the "burden" for which it seeks compensation is the burden of supporting calling facilities and activities. Now, Illinois certainly has an interest in being compensated for the burdens placed upon it by the conduct of activity and operation of facilities within its territory, such as those involved in instate calling. But, Illinois has *no* sovereign interest in being compensated for those activities occurring and facilities run outside its borders, so that it has no right to be compensated for the entirety of each interstate call, part of which invariably involves such out-of-state activity and facilities. The two

different events—instate calling and interstate calling—do not impose comparable burdens on the State. Therefore, an equal tax on the two events does not represent equal treatment, because the burdens imposed on the State by the two are not equivalent.[14]

Indeed, this Court has recognized that the imposition of equal tax rates on intra- and interstate activities does not necessarily signify that the state's taxing scheme is non-discriminatory. *American Trucking Associations, Inc. v. Scheiner*, 107 S. Ct. 2829, 2842 (1987) (facially equal taxes can nevertheless subject interstate activity to discriminatory multiple burdens). Here, the facially equal taxes are discriminatory. The interstate calls carry a tax burden the intrastate calls do not because, as to interstate calls, the activity occurring outside the state which is being taxed by Illinois is also subject to taxing by other states. Instate calls are not exposed to any such additional burdens. Therefore, the interstate calls are effectively taxed more heavily. This constitutes impermissible discrimination against interstate commerce, under *American Trucking Association, Inc. v. Scheiner*, 107 S. Ct. 2829, 2840–41 (1987) and *Tyler Pipe Industries, Inc. v. Washington State Department of Revenue*, 107 S. Ct. 2810, 2820 (1987).[15]

In any event, the issue of whether the 5%/5% tax treatment of the two different types of calls rescues the taxing statute from its otherwise discriminatory effects raises a significant issue under the Commerce Clause.

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[14] In this respect, the Illinois intra- and interstate tax scheme is totally different from a use/sales tax scheme which applies to tangible personal property sold entirely in one state and then entirely consumed within another. *Cf. Henneford v. Silas Mason Co.*, 300 U.S. 577 (1937). Interstate service simply does not represent a distinguishable and totally out-of-state counterpart to some totally instate activity, as the "use" of a product outside a state does to the sale of it within another state.

[15] As this Court has stated, "The [local] incident [of interstate

(Footnote continued on the following page)

The trial court found discrimination persisted despite this facial equality, whereas the Illinois Supreme Court did not. Goldberg App. E at 20a–24a; Goldberg App. C at 11a, 16a. This Court should resolve that disagreement.

3. The Tax Is Not Fairly Related to Services Provided by Illinois

A state tax on interstate activity must be "fairly related to the services provided by the State." *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977). GTE Sprint argued below that the Illinois tax failed this fourth *Complete Auto* test. The Illinois Supreme Court disagreed, concluding that "the services provided by [Illinois] facilitate perhaps the most critical step in the taxable event—interstate origination . . . [while] . . . the benefits afforded by other States in facilitating the same interstate telecommunication are *too speculative* to override the substantial benefits extended by Illinois." Goldberg App. C at 13a (emphasis added). But this finding has no basis in fact or law.

As to the factual basis for the Illinois court's conclusion, GTE Sprint introduced uncontroverted facts below which establish the highly significant role of states other than Illinois in facilitating interstate telecommunications, even where they begin in Illinois. *See* Statement of the Case, *supra* at 4; Sprint App. C at 7a–8a. The state court's conclusion that benefits provided by other states are "speculative" has no basis whatsoever in fact, on this record.

The court also had no legal basis for concluding that the Illinois tax has any fair relation to the support Illinois provides the taxed activity. The fair relation test requires that "the *measure* of the tax must be reasonably related

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15 *(continued)*

commerce] selected [to be taxed] should be one that does not lend itself to repeated exactions in other states. Otherwise intrastate commerce may be preferred over interstate commerce." *Memphis Natural Gas Co. v. Stone*, 335 U.S. 80, 87 (1948).

to the extent of the contact [the activity has with the taxing state], since it is the activities or presence of the taxpayer in the State that may properly be made to bear a 'just share of the state tax burden. [T]he incidence of the tax *as well as its measure* [must be] tied to the earnings which the State . . . has made possible. . . .'" *Commonwealth Edison Co. v. Montana*, 453 U.S. 609, 626 (1981) (citations omitted; emphasis added).

But the measure of the Illinois tax is in no way tied to the earnings or charges which Illinois has made possible with regard to interstate calling. The Illinois tax taxes the entire charge for any long distance call, even though it is clear that not all of that charge is attributable to activities within Illinois. Thus, there is no fair relation between the measure of the tax and the extent of Illinois activity involved in the taxed long distance calls. Further, as GTE Sprint has argued, and supported by uncontested affidavit, the Illinois tax is constitutionally perverse, so to speak, because it tends to tax a call more heavily the less the call involves Illinois activity. Specifically, since calls made over greater distances tend to cost more, GTE Sprint charges more for those calls. And the greater the distance of a call, the more out-of-state or non-Illinois activity tends to be involved. But, because Illinois receives a flat 5% on the gross charge for calls, Illinois tends to receive more revenue on calls the more expensive and longer they are and, therefore, the more they involve activity *outside* the State of Illinois. *See* Statement of the Case, *supra* at 4; Sprint App. C at 8a-9a. The tax therefore operates in direct contradiction to the dictates of the fair relation rule because there is an *inverse* relationship between the amount of Illinois activity involved in a long distance call and the measure of the tax. This insidious inverse relationship should render the Illinois tax unconstitutional. *See Commonwealth Edison Co. v. Montana*, 453 U.S. 609, 627-29 (1981). There is, at least, a substantial issue posed as to whether the Illinois tax can pass the fourth prong of the *Complete Auto* test.

II. The Imposition of the Illinois Tax Raises Substantial Issues which Are Novel, Important and Deserve Review

GTE Sprint has demonstrated that reversal of the Illinois Supreme Court judgment is likely on several grounds and that, therefore, substantial questions of constitutional law have been raised which should be addressed by this Court. But there are additional reasons for plenary review. For example, no similar state tax on long distance telephone calls has previously been evaluated by this Court. Though two state courts have recently considered and upheld the constitutionality of state taxes on long distance calls, neither decision ever reached this Court; both involved taxes which differ facially and in their application from the Illinois tax; and, in both cases, the courts based their decisions on legal premises rejected by this Court. *See* discussion *supra* at 19-20 and fn. 12. Further, despite the utter irrelevance of these prior cases to the issues presented by this appeal, the Illinois Supreme Court relied upon them in upholding the Illinois tax. Review of the issues presented by this appeal is therefore desperately needed, to clarify legal precedent and Commerce Clause law in this generally confusing area of state taxation. *See American Trucking Associations, Inc. v. Scheiner*, 107 S. Ct. 2829, 2832 (1987) (noting "uneven course of decisions" in area of Commerce Clause restrictions on state taxation); *McDaniel v. Sanchez*, 448 U.S. 1318, 1322 (1980) (Powell, Circuit Justice, in chambers) (ambiguity of precedent argues in favor of noting probable jurisdiction).

Full review of GTE Sprint's challenge to the Tax Act is also called for because of the wide-reaching impact of a decision evolving from that review. This tax challenge is important to all those who have come to depend upon the interstate transmission of speech, information, data and images — all of which could be taxed under statutes like the statute at issue here. Further, given the actual proliferation of long distance telecommunications and taxes on

those communications, *see* discussion *supra* at 8, 16-17 and fn. 10, we all need guidance on what our Commerce Clause allows. *Hicks v. Feiock*, 107 S. Ct. 259 260 (1986) (O'Connor, Circuit Justice, in chambers); *National Collegiate Athletic Association v. Board of Regents*, 463 U.S. 1311, 1313 (1983) (White, Circuit Justice, in chambers).

CONCLUSION

In conclusion, the substantiality of the federal question, the likelihood of reversal, the lack of clear precedent, the need for clear guidance, and the widespread importance of the issues raised herein all argue strongly in favor of this Court noting probable jurisdiction and reversing the judgment of the Illinois Supreme Court.

Respectfully submitted,

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APPENDICES

APPENDIX A

No. 64355

In The Supreme Court of Illinois

JEROME F. GOLDBERG and ROBERT McTIGUE, individually and on behalf of all others similarly situated, *Plaintiffs-Appellees and Cross-Appellants,* *v.* J. THOMAS JOHNSON, Director of Revenue for the Department of Revenue of the State of Illinois, *Defendant-Appellant,* *and* GTE SPRINT COMMUNICATIONS CORPORATION, et al., *Defendants.*	Direct Appeal from the Circuit Court of Cook County, Chancery Division
GTE SPRINT COMMUNICATIONS CORPORATION, *Counter-Plaintiff-Appellee,* *v.* J. THOMAS JOHNSON, Director of Revenue for the Department of Revenue of the State of Illinois, and JAMES H. DONNEWALD, Treasurer of the State of Illinois, *Defendants-Appellants.*	No. 85 CH 8081 — The Honorable Richard L. Curry, Judge Presiding

NOTICE OF APPEAL TO THE SUPREME COURT OF THE UNITED STATES

Notice is hereby given that GTE Sprint Communications Corporation, the Counter-Plaintiff-Appellee above-named, hereby appeals to the Supreme Court of the United States the judgment of the Supreme Court of Illinois entered herein on June 24, 1987.

This appeal is taken pursuant to 28 U.S.C. § 1257(2).

Respectfully submitted,

By: /s/ LAURA DI GIANTONIO
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CERTIFICATE OF SERVICE

I, Laura Di Giantonio, certify that on December 7, 1987, I caused the Notice of Appeal to the Supreme Court of the United States to be served on all those persons on the attached Service List by causing one true and correct copy to be placed, first class postage prepaid, in envelopes, correctly addressed, and sent by United States Mail.

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APPENDIX B

ILLINOIS SUPREME COURT
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October 5, 1987

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No. 64355 - Jerome F. Goldberg, et al., etc., appellees, v. J. Thomas Johnson, Director of Revenue, etc., et al., appellants. Appeal, Circuit Court (Cook).

The Supreme Court today DENIED the petition for rehearing in the above entitled cause.

The mandate of this Court will issue to the appropriate Appellate Court and/or Circuit Court or other agency on January 21, 1988.

APPENDIX C

STATE OF ILLINOIS }
COUNTY OF COOK } SS

AFFIDAVIT OF RICHARD N. WILEY

Richard N. Wiley, being over the age of 21 and being competent to testify to the matters herein, deposes and states as follows:

1. I formerly served as Tax Manager and then as Senior Tax Attorney for GTE Sprint Communications Corporation ("GTE Sprint") from 1980-1985.

2. In 1986, GTE Sprint combined with U.S. Telecom, Inc. to form a partnership known as U.S. Sprint Communications Company ("U.S. Sprint"). This partnership was formed to provide long distance telecommunications services in the United States and elsewhere.

3. I am now a General Attorney employed by U.S. Sprint.

4. In my various positions with GTE Sprint and then with U.S. Sprint, I have of necessity become familiar with the operations of those companies.

5. GTE Sprint was, prior to July 1, 1986, a retailer of intrastate and interstate telecommunications services. As U.S. Sprint it so remains. (Hereinafter GTE Sprint and U.S. Sprint will be referred to as "GTE Sprint," in the present tense.)

6. GTE Sprint's customers use its services to convey and receive voice and other messages. A large part of GTE Sprint's business centers on providing interstate voice transmission by telephone, in all fifty states of the United States and to several foreign countries. In order to provide voice transmission services, GTE Sprint has established, over the years, its own interstate transmission network comprised of microwave radio, fiber optic, satellite and

cable transmission facilities which are spread over numerous states. GTE Sprint has constructed this interstate network of transmission facilities at great expense.

7. In transmitting voice messages on an interstate basis, GTE Sprint utilizes its own facilities where possible.

8. However, GTE Sprint must utilize the services of other telecommunications carriers in some areas its lines do not reach. In such cases, GTE Sprint purchases services from these other carriers.

9. GTE Sprint is also forced to use other carriers' services at the local level since local operating companies control the facilities which are used to originate and terminate calls. For example, GTE Sprint typically pays the local exchange telephone company (usually a Bell Operating Company) at the originating end of a transmission for picking up the communication from its origin (generally the caller's telephone device) and delivering it to the GTE Sprint network. Likewise, at the terminating end of the communication, GTE Sprint typically pays another local exchange telephone company for delivering the communication from the GTE Sprint network to the point of termination.

10. The local exchange services for this purpose are termed "access services" and the charges for using the local exchange services for picking up and dropping off the message at the local level are termed "access charges."

11. Other costs are incurred by GTE Sprint in the establishment and maintenance of its own network over which its customers' calls are transmitted where possible. GTE Sprint thus incurs costs in sending its interstate transmissions, both in the cost of building and maintaining its own lines, and in purchasing services from other carriers.

12. GTE Sprint incurs transmission costs over the entire pathway of each communication. The transmis-

sion and other costs incurred are typically recovered from GTE Sprint's customers in the tariffed prices they pay for telecommunications services. The basic charge for an interstate toll call varies according to the distance between the place the call originates and the place it terminates, increasing in price as the distance between these points increases. The charge for an interstate private line call varies solely according to the length of the line utilized in the transmission.

13. GTE Sprint's intrastate telecommunications services are provided pursuant to tariffs authorized by the Illinois Commerce Commission, while its interstate telecommunications services are common carrier services provided subject to Federal Communications Commission regulation and pursuant to 47 U.S.C. § 201 *et seq.*

e14. GTE Sprint has the administrative capability to bill taxes to its customers on telecommunications services which originate in any state, or terminate in any state, or are billed in any state, or any combination of these criteria for any number of states. Specifically, GTE Sprint has the administrative capability to bill more than one state's tax to a single customer for a single communication. For example, GTE Sprint can bill an Illinois customer for an interstate telecommunication originating in Illinois and terminating in New York, and could include, in that charge, a tax assessed by Illinois, the originating state, and New York, the terminating state.

15. The first payment of the excise tax imposed by the Illinois Telecommunications Excise Tax Act was due the State of Illinois on September 15, 1985. Because of certain business and technical exigencies, GTE Sprint was not able, at that time, to implement a system to pass the tax through to its customers on their bills. Therefore, GTE Sprint undertook to remit to the State the taxes due under the Act, until such time as it could implement such a system. GTE Sprint made a number of the tax payments

itself thereafter, until it was finally able to implement a system to pass the tax on to its customers, around October or November, 1985.

16. From September 15, 1985 to the present, GTE Sprint has paid to the State of Illinois a total of $ 2,146,904.28 in taxes due the State by its customers for interstate telecommunications services, at least $ 391,568.00 of which has been paid by Sprint itself, and not its customers, due to Sprint's temporary administrative inability to pass along the tax.

17. These payments GTE Sprint has made under protest, pursuant to Illinois statutory provision, in order to preserve its right to a refund of those payments should the Tax Act ultimately be declared unconstitutional in this lawsuit.

18. GTE Sprint has met all the requirements for requesting a refund under the Money Disposition Act, as it filed suit challenging the tax within the specified time period, obtained the required injunction, and has paid over the tax to the State, under protest, and accompanied by the required protest form.

/s/ RICHARD N. WILEY
Richard N. Wiley

Subscribed and sworn to
before me this 25th day
of July, 1986.

/s/ COLLEEN C. JARDINE
Notary Public
[Seal]

APPENDIX D

FLORIDA SALES TAX

212.05. Sales, storage, use tax

It is hereby declared to be the legislative intent that every person is exercising a taxable privilege who engages in the business of selling tangible personal property at retail in this state, or who rents or furnishes any of the things or services taxable under this chapter, or who stores for use or consumption in this state any item or article of tangible personal property as defined herein and who leases or rents such property within the state.

(1) For the exercise of such privilege, a tax is levied on each taxable transaction or incident, which tax is due and payable as follows:

* * * *

(e)1. At the rate of 5 percent on charges for all telegraph messages and long distance telephone calls beginning and terminating in this state; on charges for telecommunication service as defined in s. 203.012 and for those services described in s. 203.012(2)(a); on recurring charges to regular subscribers for wired television service; on all charges for the installation of telecommunication, wired television, and telegraphic equipment; and on all charges for electrical power or energy. For purposes of this subparagraph, the term "telecommunication service" does not include local service provided through a pay telephone. The provisions of s. 212.17(3), regarding credit for tax paid on charges subsequently found to be worthless, shall be equally applicable to any tax paid under the provisions of this section on charges for telecommunication or telegraph services or electric power subsequently found to be uncollectible. The word "charges" in this paragraph does not include any excise or similar tax levied by the Federal Government, any political subdivision of the state, or any municipality upon the purchase or sale of telecommunica-

tion, wired television, or telegraph service or electric power, which tax is collected by the seller from the purchaser.

2. Telegraph messages and telecommunication services which originate or terminate in this state, other than interstate private communication services, and are billed to a customer, telephone number, or device located within this state are taxable under this paragraph. Interstate private communication services are taxable under this paragraph as follows:

a. One hundred percent of the charge imposed at each channel termination point within this state;

b. One hundred percent of the charge imposed for the total channel mileage between each channel termination point within this state; and

c. The portion of the interstate interoffice channel mileage charge as determined by multiplying said charge times a fraction, the numerator of which is the air miles between the last channel termination point in this state and the vertical and horizontal coordinates, 7856 and 1756, respectively, and the denominator of which is the air miles between the last channel termination point in this state and the first channel termination point outside this state. The denominator of this fraction shall be adjusted, if necessary, by adding the numerator of said fraction to similarly determined air miles in the state in which the other channel termination point is located, so that the summation of the apportionment factor for this state and the apportionment factor for the other state is not greater than one, to ensure that no more than 100 percent of the interstate interoffice channel mileage charge can be taxed by this state and another state.

3. The tax imposed pursuant to this paragraph shall not exceed $50,000 per calendar year on charges to any person for interstate telecommunications services defined in s. 203.012(4) and (7)(b), if the majority of such services used by such person are for communications originating

outside of this state and terminating in this state. This exemption shall only be granted to holders of a direct pay permit issued pursuant to this subparagraph. No refunds shall be given for taxes paid prior to receiving a direct pay permit. Upon application, the department may issue a direct pay permit to the purchaser of telecommunications services authorizing such purchaser to pay tax on such services directly to the department. Any vendor furnishing telecommunications services to the holder of a valid direct pay permit shall be relieved of the obligation to collect and remit the tax on such service. Tax payments and returns pursuant to a direct pay permit shall be monthly. For purposes of this subparagraph, the term "person" shall be limited to a single legal entity and shall not be construed as meaning a group or combination of affiliated entities or entities controlled by one person or group of persons. For purposes of this subparagraph, for calendar year 1986, the term "calendar year" means the last 6 months of 1986.

APPENDIX E

ORDINANCE NO. 630

BE IT ORDAINED BY THE CITY COUNCIL OF THE CITY OF WHEAT RIDGE, COLORADO THAT:

Section 1. Section 21-1 – Definitions of the Code of Laws of the City of Wheat Ridge is amended by the addition of the following definitions:

"LOCAL EXCHANGE COMPANY" means any person which provides public telephone or telecommunication exchange access lines, mobile telecommunications or channels necessary to effect the transfer of two-way voice or data grade information between the final user and the local telecommunications network.

"TELECOMMUNICATIONS SERVICE" means the transport of signs, signals, writings, images, sounds, messages, data, or other information of any nature by wire, radio, light waves, electromagnetic, digital, or electronic means.

"ACCESS SERVICES" means any charge by local telephone exchange companies to providers of telecommunications services for use in providing their telecommunications services.

Section 2. Section 21-4 - Property and Services Subject to Tax of the Code of Laws of the City of Wheat Ridge is amended by the repeal and reenactment of the following provisions thereof:

There is hereby levied and there shall be collected and paid a tax in the amount stated in Section 21-7 as follows: on all sales and services taxable by the State of Colorado under the sales tax provisions of the Colorado Revised Statutes 1973, 39-26-104, as amended, including, not limited to the following:

(b) UPON TELECOMMUNICATIONS SERVICES, EXCEPT ACCESS SERVICES AS DESIGNATED IN SECTION 21-5(8), WHETHER FURNISHED BY PUBLIC OR PRIVATE CORPORATIONS OR ENTERPRISES FOR ALL INTERSTATE AND INTRASTATE TELECOMMUNICATIONS SERVICE ORIGINATING FROM OR RECEIVED ON TELECOMMUNICATIONS EQUIPMENT IN THIS CITY IF THE CHARGE FOR THE SERVICE IS BILLED TO A PERSON IN THIS CITY OR BILLED TO AN AFFILIATE OR DIVISION OF SUCH PERSON IN ANY STATE/CITY ON BEHALF OF A PERSON IN THIS CITY.

Section 3. Section 21-5. Same - Exempt of the Code of Laws of the City of Wheat Ridge is hereby amended by the addition of the following subpart 21-5(i) (8):

(8) "ACCESS SERVICES" BY LOCAL TELEPHONE EXCHANGE COMPANIES TO PROVIDERS OF TELECOMMUNICATIONS SERVICE FOR USE IN PROVIDING SUCH SERVICE SHALL BE DEEMED TO BE WHOLESALE SALES AND SHALL BE EXEMPT FROM TAXATION UNDER THIS SECTION.

SIGNED by the Mayor on this 12th day of August, 1985.

/s/ Frank Stites
Frank Stites, Mayor

ATTEST:
/s/ Wanda Sang
Wanda Sang, City Clerk

APPENDIX F

CITY OF GREELEY, COLORADO
ORDINANCE NO. 45, 1985

NOW, THEREFORE, BE IT ORDAINED BY THE CITY COUNCIL OF THE CITY OF GREELEY, COLORADO:

Section 1. Section 4.04.060 of the Code of Ordinances, a copy of which is attached hereto, marked "Exhibit A" and incorporated herein by reference, is amended to read as follows:

4.04.060 Sales tax–Levied. There is levied and there shall be collected and paid a tax in the amount stated in Section 4.04.145 as follows:

C. Upon telecommunications services, except access services as designated in Section 4.04.015 (S), whether furnished by public or private corporations or enterprises for all interstate and intrastate telecommunications services originating from or received on telecommunications equipment in this city if the charge for the service is billed to a person in this city or billed to an affiliate or division of such person in any state or any other city in this state on behalf of a person in this state;

R. "Telecommunications Service" means the transport of signs, signals, writing, images, sounds, messages, data, or other information of any nature by wire, radio, light waves, electromagnetic, digital, or electronic means.

S. "Access Services" means any charge by local telephone exchange companies to providers of telecommunications services for use in providing their telecommunications services.

Section 2. This Ordinance shall become effective on July 1, 1985.

PASSED AND ADOPTED, SIGNED AND APPROVED THIS 7th DAY OF May, 1985.

ATTEST: THE CITY OF GREELEY, COLORADO

/s/ Gayle Voss
City Clerk

By: /s/ Mike Lehan
Mayor

APPENDIX G

WASHINGTON BUSINESS AND OCCUPATION TAX

82.04.050. "Sale at retail", "retail sale"

(1) "Sale at retail" or "retail sale" means every sale of tangible personal property (including articles produced fabricated, or imprinted) to all persons irrespective of the nature of their business and including, among others, without limiting the scope hereof, persons who install, repair, clean, alter, improve, construct, or decorate real or personal property of or for consumers other than a sale to a person who (a) purchases for the purpose of resale as tangible personal property in the regular course of business without intervening use by such person, or (b) installs, repairs, cleans, alters, imprints, improves, constructs, or decorates real or personal property of or for consumers, if such tangible personal property becomes an ingredient or component of such real or personal property without intervening use by such person, or (c) purchases for the purpose of consuming the property purchased in producing for sale a new article of tangible personal property or substance, of which such property becomes an ingredient or component or is a chemical used in processing, when the primary purpose of such chemical is to create a chemical reaction directly through contact with an ingredient of a new article being produced for sale, or (d) purchases for the purpose of consuming the property purchased in producing ferrosilicon which is subsequently used in producing magnesium for sale, if the primary purpose of such property is to create a chemical reaction directly through contact with an ingredient of ferrosilicon, or (e) purchases for the purpose of providing the property to consumers as part of competitive telephone service, as defined in RCW 82.04.065. There term shall include every sale of tangible personal property which is used or consumed or to be used or consumed in the performance of any activity classified as a "sale at retail" or "retail sale" even though such property is resold or utilized as provided in (a), (b), (c), (d), or (e) above following

such use. The term also means every sale of tangible personal property to persons engaged in any business which is taxable under RCW 82.04.280, subsections (2) and (7) and RCW 82.04.290.

* * * *

(5) The term shall also include the providing of telephone service, as defined in RCW 82.04,065, to consumers.

* * * *

82.04.065. "Competitive telephone service", "network telephone service", "telephone service", "telephone business"

(1) "Competitive telephone service" means the providing by any person of telecommunications equipment or apparatus or service related to that equipment or apparatus such as repair or maintenance service, if the equipment or apparatus is of a type which can be provided by persons that are not subject to regulation as telephone companies under Title 80 RCW and for which a separate charge is made.

(2) "Network telephone service" means the providing by any person of access to a local telephone network, local telephone network switching service, toll service, or coin telephone services, or the providing of telephonic, video, data, or similar communication or transmission for hire, via a local telephone network, toll line or channel, cable, microwave, or similar communication or transmission system. "Network telephone service" includes interstate service, including toll service, originating from or received on telecommunications equipment or apparatus in this state if the charge for the service is billed to a person in this state. "Network telephone service" does not include the providing of competitive telephone service, the providing of cable television service, nor the providing of broadcast services by radio or television stations.

(3) "Telephone service" means competitive telephone

service or network telephone service, or both, as defined in subsections (1) and (2) of this section.

(4) "Telephone business" means the business of providing network telephone service, as defined in subsection (2) of this section. It includes cooperative or farmer line telephone companies or associations operating an exchange.

* * * *

82.04.250 Tax on retailers

Upon every person except persons taxable under RCW 82.04.260(8) engaging within this state in the business of making sales at retail, as to such persons, the amount of tax with respect to such business shall be equal to the gross proceeds of sales of the business, multiplied by the rate of forty-four one-hundredths of one percent.

APPENDIX H

NEW MEXICO GROSS RECEIPTS TAX

7-9-3. Definitions. (Effective until July 1, 1988.)

As used in the Gross Receipts and Compensating Tax Act [this article]:

* * * *

F. "gross receipts" means the total amount of money or the value of other consideration received from selling property in New Mexico, from leasing property employed in New Mexico or from performing services in New Mexico and includes any receipts from sales of tangible personal property handled on consignment but excludes cash discounts allowed and taken, New Mexico gross receipts tax payable on transactions for the reporting period and taxes imposed pursuant to the provisions of the County Sales Tax Act, the County Fire Protection Excise Tax Act, the County Gross Receipts Tax Act, the Municipal Gross Receipts Tax Act or the Supplemental Municipal Gross Receipts Tax Act which are payable on transactions for the reporting period and any type of time-price differential.

* * * *

"Gross receipts" also includes amounts paid by members of any cooperative association or similar organization for sales or leases of personal property or performance of services by such organization and amounts received from transmitting messages or conversations by persons providing telephone or telegraph services, including interstate and international messages or conversations that either originate or terminate in New Mexico and are billed to a New Mexico telephone number or account;

7-9-4. Imposition and rate of tax; denomination as "gross receipts tax".

A. For the privilege of engaging in business, an excise

tax equal to four and three-fourths percent of gross receipts is imposed on any person engaging in business in New Mexico.

B. The tax imposed by this section shall be referrred to as the "gross receipts tax".

* * * *

7-9-55. Deduction; gross receipts tax; transaction in interstate commerce. (Effective until July 1, 1988.)

Receipts from transactions in interstate commerce may be deducted from gross receipts to the extent that the imposition of the gross receipts tax would be unlawful under the United States constitution.

Receipts from transmitting messages or conversations by radio other than from one point in this state to another point in this state and receipts from the sale of radio or television broadcast time when the advertising message is supplied by or on behalf of a national or regional seller or advertiser not having its principal place of business in or being incorporated under the laws of this state, may be deducted from gross receipts. Commissions of advertising agencies from performing services in this state may not be deducted from gross receipts under this section.

7-9-55. Deduction; gross receipts tax; transaction in interstate commerce. (Effective July 1, 1988.)

Receipts from transactions in interstate commerce may be deducted from gross receipts to the extent that the imposition of the gross receipts tax would be unlawful under the United States constitution.

Receipts from transmitting messages or conversations by telegraph, telephone or radio other than from one point in this state to another point in this state and receipts from the sale of radio or television broadcast time when the advertising message is supplied by or on behalf of a

national or regional seller or advertiser not having its principal place of business in or being incorporated under the laws of this state, may be deducted from gross receipts. Commissions of advertising agencies from performing services in this state may not be deducted from gross receipts under this section.

7-9-56. Deduction; gross receipts tax; intrastate transportation and services in interstate commerce. (Effective until July 1, 1988.)

* * * *

C. Receipts from providing telephone or telegraph services in this state which will be used by other persons in providing telephone or telegraph services to the final user and thirty-five percent of the receipts of persons providing interstate and foreign telephone or telegraph services from transmitting interstate messages or conversations may be deducted from gross receipts.

Nos. 87-826, 87-1101

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

JEROME F. GOLDBERG and ROBERT McTIGUE,
Appellants,

v.

ROGER D. SWEET, DIRECTOR OF THE ILLINOIS DEPARTMENT OF REVENUE, et al.,
Appellees.

GTE SPRINT COMMUNICATIONS CORPORATION,
Appellant,

v.

ROGER D. SWEET, DIRECTOR OF THE ILLINOIS DEPARTMENT OF REVENUE, et al.,
Appellees.

On Appeal From The Supreme Court Of Illinois

CONSOLIDATED MOTION TO AFFIRM

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On Appeal From The Supreme Court Of Illinois

CONSOLIDATED MOTION TO AFFIRM

Appellees Roger D. Sweet, Director of the Illinois Department of Revenue and Jerome Cosentino, Treasurer of the State of Illinois (the "Department of Revenue"), move to affirm the decision of the Illinois Supreme Court

pursuant to United States Supreme Court Rule 16.[1] In the decision below, the Illinois Supreme Court properly applied this Court's precedents. The questions presented by the appeals are so unsubstantial that there is no need for further argument.

STATEMENT OF THE CASE

Appellants Jerome Goldberg and Robert McTigue filed suit in the Circuit Court of Cook County, Illinois, alleging that Section 4 of the Illinois Telecommunications Excise Tax Act, Ill. Rev. Stat. ch. 120, paras. 2001-2104 (1986) (the "Act"), violated the Commerce Clause of the Constitution of the United States. U.S. Const. art. I, § 8, cl. 3. Appellant GTE Sprint Communications Corporation ("GTE"), a defendant in the Circuit Court suit, filed a cross-claim against the Department of Revenue based on the same alleged constitutional infirmity.[2] Section 4 of the Act states:

> A tax is imposed upon the act or privilege of originating in this State or receiving in this State interstate telecommunications by a person in this State at the rate of 5% of the gross charge for such telecommunications purchased at retail from a retailer by such person. To prevent actual multi-state taxation of the act or privilege that is subject to taxation under this paragraph, any taxpayer, upon proof that that taxpayer has paid a tax in another state on such event, shall be allowed a credit against the tax imposed in this Section 4 to the extent of the amount of such tax properly due and paid in such other state. However, such tax is not imposed on the act or privilege to the extent such act or privilege may not, under the Constitution and statutes of the United States, be made the subject of taxation by the State.

Ill. Rev. Stat. ch. 120, para. 2004 (1986).[3]

On cross motions for summary judgment seeking a determination of the constitutionality of Section 4 of the Act, the Circuit Court of Cook County, Illinois, held that this provision violated the Commerce Clause of the United States Constitution. (Goldberg App. at 18a-24a.) Thereafter, in accordance with the Illinois Supreme Court Rules, the Department of Revenue took a direct appeal of the Circuit Court's decision to the Illinois Supreme Court. On June 24, 1987, the Illinois Supreme Court issued an order reversing the Circuit Court and finding the Act constitutional. (Goldberg App. at 17a.) On July 27, 1987, the Illinois Supreme Court issued an opinion explaining its June 24, 1987 order. *Goldberg v. Johnson*, 117 Ill. 2d 493, 512 N.E.2d 1262 (1987). (Goldberg App. at 4a-16a.) As is demonstrated below, the Illinois Supreme Court properly applied the law, and further review of this straightforward statute is not warranted.

[1] This Motion to Affirm responds to the Jurisdictional Statements filed by Jerome F. Goldberg and Robert McTigue in Case No. 87-826 and GTE Sprint Communications Corporation in Case No. 87-1101. These Jurisdictional Statements shall be referred to as the "Goldberg Jurisdictional Statement" and the "GTE Jurisdictional Statement," respectively. The appendices attached to the Goldberg Jurisdictional Statement shall be referred to as "Goldberg App."

[2] Appellants also raised due process and equal protection claims under the United States and Illinois Constitutions which they have abandoned on their appeals.

[3] The Act, in Section 2, defines "gross charge" as "the amount paid . . ." and "amount paid" as "the amount charged to the taxpayer's service address in this State regardless of where such amount is billed or paid." Ill. Rev. Stat. ch. 120, para. 2002(a), (b) (1986).

ARGUMENT

A. The Act Taxes Illinois Activity.

The events that give rise to the tax occur in Illinois. A tax is imposed only when (i) a person in Illinois originates or receives a telephone call; (ii) a person in Illinois decides to charge the cost of that call to an Illinois service address; and (iii) the call is purchased at retail in Illinois. Although these activities take place in Illinois, they have sufficient interstate implications so that the tax imposed by the Act is subject to scrutiny under the standards set forth by this Court in *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, *reh'g denied*, 430 U.S. 976 (1977) and its progeny. The Illinois Supreme Court's definition of the "taxable event" demonstrates that it understood that acts which are local in nature can have interstate implications:

> Since the taxable event in this case is the "act or privilege of originating or receiving interstate telecommunications * * * in this State," it is clear that the taxable event is linked inextricably to interstate activity—interstate communication.

512 N.E.2d at 1265. (Goldberg App. at 9a.) While the activity of originating or receiving a telephone call is "linked" to interstate commerce, it is not interstate activity in and of itself.

Appellants' Jurisdictional Statements mischaracterize the Illinois Supreme Court's construction of the Act and disregard the practical application of the Act by arguing that the Act places a direct tax on interstate telephone calls. Appellants' analysis ignores the essential Illinois economic activity the Act requires in order to impose any tax. Appellants Goldberg and McTigue argue that "the tax is unquestionably imposed on the interstate telephone call itself." (Goldberg Jurisdictional Statement at 12 n.6.) Appellant GTE states that "the tax has clearly been laid on inherently interstate activity." (GTE Jurisdictional Statement at 9.) Appellants choose to completely ignore the fact that both the Act and the Illinois Supreme Court define the taxable event to include the origination or receipt in Illinois of a telephone call--singularly local events.[4]

In evaluating the interplay between state taxation and the Commerce Clause, this Court has repeatedly stated that the practical effect of a tax, rather than its name or label, should be utilized. *Commonwealth Edison Co. v. Montana*, 453 U.S. 609, 615-17, *reh'g denied*, 453 U.S. 927 (1981); *American Trucking Ass'ns, Inc. v. Scheiner*, ____ U.S. ____, 107 S. Ct. 2829, 2846 (1987). The practical effect of the Act can be shown by a series of examples. Under the Act, a caller who makes a direct dial call from Illinois to California, and is charged for that call at an Illinois service address, is subject to taxation. Similarly, a person in Illinois who accepts a collect call from California which is charged to an Illinois service address, is subject to taxation. However, a person who makes a collect call from Illinois to California, and thus is not charg-

[4] Appellant GTE further confuses the issues by arguing that "the tax cannot be deemed to tax a local 'sales' transaction, as it explicitly taxes long distance calls even when they are *billed and/or are paid for outside Illinois.*" (Emphasis in original.) (GTE Jurisdictional Statement at 10.) A simple example displays the fallacy in this argument. When one uses a credit card to purchase items during an out-of-state trip, one may be required to pay a sales tax to the state in which the purchase is made. The fact that the credit card bill is thereafter received in another state and paid there does not prevent, as GTE has argued, the tax from being a tax on a local sale.

ing the call to a service address in Illinois, is not subject to taxation. A person making a long distance directory assistance call originated in Illinois is taxed only when there is a charge to an Illinois service address. As is demonstrated by the foregoing examples, it is not the existence of a telephone call that triggers the tax. No tax arises, under the Act, in the absence of a decision by a person participating in a telephone call while in Illinois to have the call charged to an Illinois service address.

Appellants Goldberg and McTigue also argue that Illinois is taxing the "entire call," thereby taxing interstate activity. It is important to recognize that the Act has the effect of taxing the entire charge for the call only when a telephone company elects to place the entire charge on the Illinois participant. If a telephone company chooses to divide the charges for telephone services between the originator and the recipient, the Act would tax only the amount charged to an Illinois service address, leaving untaxed the amount charged in another state.

B. The Illinois Supreme Court Followed This Court's Recent Precedents.

The Act imposes an uncomplicated tax which relates directly to Illinois economic activity. It is designed to satisfy the established precedents of this Court. The most recent decisions of the Supreme Court regarding the relationship of the Commerce Clause to state taxes, which were decided subsequent to the enactment of the Act, provide additional support for the constitutionality of the Act.

In 1987, this Court rendered two opinions deciding challenges to state taxes under the Commerce Clause. In *Tyler Pipe Industries, Inc. v. Washington State Department of Revenue,* ____ U.S. ____, 107 S. Ct. 2810 (1987)

and *American Trucking Ass'ns, Inc. v. Scheiner,* ____ U.S. ____, 107 S. Ct. 2829 (1987), this Court struck down Washington and Pennsylvania statutes as unconstitutional burdens on interstate commerce. The infirmities of those statutes are not present in the Act, but the reasoning of this Court was relied upon by the Illinois Supreme Court in upholding the Act.

In *Tyler Pipe,* this Court found a Washington taxing scheme, which had the practical effect of favoring Washington manufacturers, unconstitutional. The Act contains no such local favoritism. The Illinois Supreme Court, however, utilized the logic of *Tyler Pipe* in determining that the Act did not impose improper multiple taxation. Further, the Illinois Supreme Court properly analyzed a credit provision contained in the Act on the basis of *Tyler Pipe,* 512 N.E.2d at 1267. (Goldberg App. at 13a.)

In *American Trucking,* this Court held unconstitutional certain flat taxes on trucks which traveled in the Commonwealth of Pennsylvania. This Court found that the Pennsylvania taxing scheme failed the internal consistency test. This test is used to determine the existence of discrimination against interstate commerce by measuring whether a tax treats interstate and intrastate commerce equally. If the tax imposed by Pennsylvania were imposed in all fifty states, a truck which traveled in all states would pay fifty times more tax than a truck which stayed in Pennsylvania, even if each truck traveled the same number of miles. Therefore, the Pennsylvania statutes imposed an impermissible burden on interstate commerce. Conversely, if the Act were imposed in every state, a caller placing interstate telephone calls from each of the fifty states would pay exactly the same tax as a caller who placed interstate calls with identical charges exclusively from Illinois. Nothing in the Act interdicts the holding of *American Trucking.*

This appeal presents no special issues which need to be addressed by this Court. The Act imposes a garden variety tax on local activity which has interstate implications. It has none of the infirmities of the taxes reviewed in *Tyler Pipe* or *American Trucking* and fully satisfies this Court's established tests.

C. The Act Satisfies the Requirements Imposed by *Complete Auto Transit, Inc. v. Brady.*

In *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, *reh'g denied*, 430 U.S. 976 (1977), this Court set forth a four part test to apply to taxes attacked as undue burdens on interstate commerce. The *Complete Auto* test, as it has been applied, holds that a tax will not violate the Commerce Clause so long as it:

> 1. Is applied to an activity with a substantial nexus with the taxing state;
>
> 2. Is fairly apportioned;
>
> 3. Does not discriminate against interstate commerce; and
>
> 4. Is fairly related to the services provided by the state imposing the tax.

430 U.S. at 278-79.

Appellants have conceded that there is nexus. As is shown below, there is no substantial question regarding apportionment, discrimination, or fair relation.

1. The Act Imposes a Fairly Apportioned Tax.

Fair apportionment can include 100% apportionment in the taxing state. *Commonwealth Edison Co. v. Montana*, 253 U.S. 609, *reh'g denied*, 453 U.S. 927 (1981). *Complete Auto* does not require that a tax imposed on a particular

aspect of interstate commerce be spread among several states. Flexibility in apportionment is allowed so long as intrastate commerce is not favored over interstate commerce. *Container Corporation of America v. Franchise Tax Board*, 463 U.S. 159, 180-84, *reh'g denied*, 464 U.S. 909 (1983).

The propriety of 100% apportionment is illustrated by typical sales and use tax schemes employed by many states. This Court has validated the constitutionality of such taxes. *National Geographic Society v. California Board of Equalization*, 430 U.S. 551, 555 (1977). Here, the events that give rise to the tax occur exclusively in Illinois. The Act places no greater burden on interstate commerce than does a tax on the purchase of a tangible item apportioned 100% to the State where the item is purchased.

The most directly applicable decision of this Court is *Commonwealth Edison Co. v. Montana*, 453 U.S. 609, *reh'g denied*, 453 U.S. 927 (1981). There, four Montana coal producers and eleven of their out-of-state utility customers filed suit seeking refunds for the payment of a state tax on the severance of coal. The tax was "levied at varying rates depending on the value, energy content, and method of extraction of the coal, and may equal, at a maximum, 30% of the 'contract sales price.'" *Id.* at 613. The *Complete Auto* test was used to uphold this tax. With respect to fair apportionment, this Court stated: "Nor is there any question here regarding apportionment or potential multiple taxation, for as the state court observed, 'the severance can occur in no other state' and 'no other state can tax the severance.'" *Id.* at 617. The Supreme Court validated a tax which was 100% apportioned to Montana, even though the amount of the tax could not be finally determined without the participation of an out-of-state purchaser to establish the "contract sales price."

Commonwealth Edison is controlling. Here, although the election by a person in Illinois to engage in the act of originating or receiving an interstate telephone call has interstate implications, the tax imposed is fairly apportioned because it is based upon activity by a person in Illinois and charges incurred in Illinois. It bears repeating that the Act imposes a tax only where (i) a call is originated or received in Illinois; (ii) a call is charged to an Illinois service address; and (iii) the call is purchased at retail in Illinois. The fact that the rate of the Illinois tax is a percentage of the charges which are related to out-of-state activity is sufficient to subject the tax to Commerce Clause scrutiny. However, this method of determining the tax imposed by the Act is no different than the method employed by the Montana tax, approved in *Commonwealth Edison*, which was based on the value of the contract sales price to out-of-state utilities.

2. The Tax Imposed by the Act Does Not Discriminate Against Interstate Commerce.

Complete Auto requires that a state taxing statute not discriminate against interstate commerce. In *Boston Stock Exchange v. State Tax Commission*, 429 U.S. 318 (1977), this Court found a New York taxing scheme which imposed a higher tax on interstate securities transactions than on intrastate transactions discriminatory. The Court characterized the tax as the type of local favoritism that the Commerce Clause was designed to prevent. *Id.* at 329. The Act passes this important anti-discrimination test. Purchasers of intrastate telephone calls are not favored. An identical tax rate of 5% is imposed on purchasers of interstate and intrastate telephone calls and there are no exemptions or exceptions favoring intrastate telephone calls. Ill. Rev. Stat. ch. 120, para. 2003 (1986).

In *Commonwealth Edison*, this Court recognized that taxes which impose the same rate without regard to whether the transaction crosses state lines do not result in discrimination.

> [T]he Montana tax is computed at the same rate regardless of the final destination of the coal, and there is no suggestion here that the tax is administered in a manner that departs from this evenhanded formula.
>
> * * *
>
> Instead, the gravamen of appellants' claim is that a state tax must be considered discriminatory for purposes of the Commerce Clause if the tax burden is borne primarily by out-of-state consumers.
>
> * * *
>
> The premise of our discrimination cases is that "[t]he very purpose of the Commerce Clause was to create an area of free trade among the several States." Under such a regime, the borders between the States are essentially irrelevant. As the Court stated in *West v. Kansas Natural Gas Co.*, 221 U.S. 229, 255, 31 S.Ct. 564, 571, 55 L.Ed. 716 (1911), " 'in matters of foreign and interstate commerce there are no state lines.' " Consequently, to accept appellants' theory and invalidate the Montana tax solely because most of Montana's coal is shipped across the very state borders that ordinarily are to be considered irrelevant would require a significant and, in our view, unwarranted departure from the rationale of our prior discrimination cases.

453 U.S. at 618-19 (citations omitted).

Recent Supreme Court opinions have also demanded that state taxes be internally consistent so as to avoid discrimination against interstate commerce. In *Armco v. Hardesty*, 467 U.S. 638, 644, *reh'g denied*, 469 U.S. 912 (1982), this Court explained that the doctrine of internal consistency requires that if the tax at issue were imposed

by each state, interstate commerce would be subjected to no greater burden than intrastate commerce. The Act passes the *Armco* internal consistency test. If each, or any, of the other states enacted the tax in question—a tax on a person originating or receiving a call in that state and charging the call to a service address in that state—there would be no discriminatory impact upon interstate commerce.

Appellants also discuss a number of taxes now being imposed by other jurisdictions from which they conclude that the threat of multiple taxation is real, not imagined. This argument is insufficient to strike down the Act because no other jurisdiction has an adequate basis to tax the person who is in Illinois during the telephone call and charges the telephone call to an Illinois address. The fact that there may be more than one tax on different taxpayers involved in an interstate chain of events does not render the Act unconstitutional. This Court recognized in *Tyler Pipe* that taxing different aspects of the same activity is permissible when it stated:

> This apportionment argument rests on the erroneous assumption that through the B & O tax, Washington is taxing the unitary activity of manufacturing and wholesaling. We have already determined, however, that the manufacturing tax and wholesaling tax are not compensating taxes for substantially equivalent events in invalidating the multiple activities exemption. Thus, the activity of wholesaling—whether by an in-state or an out-of-state manufacturer—must be viewed as a separate activity conducted wholly within Washington that no other State has jurisdiction to tax. See *Moorman Mfg. Co. v. Bair*, 437 U.S., at 280-281, 98 S. Ct., at 2348-2349 (gross receipts tax on sales to customers within state would be "plainly valid"); *Standard Pressed Steel Co. v. Washington Revenue Dept.*, 419 U.S., at 564, 95 S. Ct., at 709 (selling tax measured by gross proceeds of sales is "apportioned exactly to the activities taxed").

___ U.S. ___, 107 S. Ct. at 2822. The Act does not impose a multiple burden because the Illinois activity which is taxed is separate from the activity which other states might try to reach.

Finally, the Act itself contains a provision which allows any taxpayer who actually suffers a multiple taxation burden to obtain a credit. There is no reason why this provision should not be treated the same as the credit provisions in sales and use tax schemes which have been upheld by this Court. Most recently, in *Tyler Pipe* this Court acknowledged the validity of credit provisions such as the one in the Act. 107 S. Ct. at 2819 n.13.

Appellant GTE rejects the credit procedure as creating an excessive administrative burden and claims that the impact of the credit provision will vary with the rates imposed by other taxing authorities, thereby creating an imperfect solution. The credit provision is not complex, but is standard for state taxes. The fact that the credit is in the amount of the tax paid to some other state is wholly consistent with the type of credit which was discussed with approval in *Tyler Pipe*, 107 S. Ct. at 2819. With the credit provision in place, the threat of any person bearing a multiple tax burden is eliminated.[5]

[5] This case does not present an appropriate vehicle for challenging the effectiveness of the credit provision of the Act because the existence of actual multiple burdens is not demonstrated in the record. While the record discloses municipal ordinances and state statutes from states other than Illinois, the actual application of those foreign ordinances and the credit provision to a particular taxpayer in Illinois and the resulting impermissible multiple burden is not shown in this record.

Appellants Goldberg and McTigue argue that there will be multiple taxation because out-of-state participants in conversations with Illinois callers could have a tax imposed on a telephone call which is covered by the Act. Appellants argue that this would lead to discrimination against interstate telephone callers because both participants in the interstate telephone call would be taxed while only one person would be taxed in an Illinois intrastate call. Appellants argument is flawed because it hypothesizes the adoption of a tax in every state other than Illinois. If both the Act and the hypothetical tax on the second participant are assumed to have been adopted in every state including Illinois, as they must be for such a hypothetical analysis under the internal consistency test, no discrimination exists.

The Act is not discriminatory because it imposes the same rate of tax on intrastate and interstate calls and because it passes the internal consistency test developed by this Court.

3. The Tax Imposed by the Act is Fairly Related to Services Provided by Illinois.

Commonwealth Edison Co. v. Montana, 453 U.S. 609, *reh'g denied*, 453 U.S. 927 (1981), establishes the standard for determining whether a state tax is fairly related to services provided by the state. *Commonwealth Edison* validated a Montana tax on the severance of coal which could be at a rate as high as 30% of the contract sales price. Here, Illinois imposes a tax equal to 5% of the purchase price. The Supreme Court recognized in *Commonwealth Edison* that the tax was "a general revenue tax" as to which the state had "considerable latitude." 453 U.S.

621-23.[6] In evaluating such taxes, this Court has made it clear that there need not be a strict relationship between the amount of tax paid and the benefit to the individual taxpayer:

> This Court has indicated that States have considerable latitude in imposing general revenue taxes . . . . [T]here is no requirement under the Due Process Clause that the amount of general revenue taxes collected from a particular activity must be reasonably related to the value of the services provided to the activity.
>
> * * *
>
> "A tax is not an assessment of benefits. It is, as we have said, a means of distributing the burden of the cost of government. The only benefit to which the taxpayer is constitutionally entitled is that derived from his enjoyment of the privileges of living in an organized society, established and safeguarded by the devotion of taxes to public purposes.
>
> Any other view would preclude the levying of taxes except as they are used to compensate for the burden on those who pay them, and would involve abandonment of the most fundamental principle of government—that it exists primarily to provide for the common good."

453 U.S. at 622-24 (citations omitted).

The Act is based on the taxpayer's activity in Illinois. The Act does not impose a tax on a party outside of Illinois and is related to the activity of the person who incurs the tax by charging a telephone call to a service address in Illinois. It is based on the value the person in Illinois places upon this activity measured by the amount

[6] Section 1 of the Act provides that "the net proceeds from the taxes imposed by this Act shall be used for the support of the General Revenue Fund." Ill. Rev. Stat. ch. 120, para. 2001 (1986).

he is willing to pay for a telephone call. It is, therefore, fairly related to activity in Illinois.

4. If the Tax Imposed by the Act is a Tax on Telephone Calls, It is Properly Apportioned.

Accepting for purposes of argument the construction of the Act argued for by all Appellants, that the Act is a tax directly on the telephone call, the Illinois statute is constitutional. Appellants' reading of the Act has no effect on the nexus, discrimination or fair relation tests, all of which are satisfied in the same manner as if the tax is viewed as one on Illinois activity.

However, with respect to the apportionment test, if Illinois is viewed as taxing interstate telephone calls, it would have sufficient nexus to reach all telecommunications which (i) originate in, (ii) are received in, or (iii) pass through Illinois. Viewed in this context, the Act is an apportioned tax on all interstate calls touching Illinois using a single apportionment factor, sales.

A tax apportioned by sales passes relevant constitutional standards. In *Moorman Mfg. Co. v. Bair,* 437 U.S. 267, *reh'g denied,* 439 U.S. 885 (1978), an Illinois corporation with sales in Iowa challenged Iowa's single factor sales method of apportionment for state income taxes. In rejecting this challenge, the Supreme Court acknowledged that a tax on activity relating exclusively to plaintiff's sales in Iowa would not run afoul of the Commerce Clause apportionment standard:

> Finally, it would be an exercise in formalism to declare appellant's income tax assessment unconstitutional based on speculative concerns with multiple taxation. For it is evident that appellant would have had no basis for complaint if, instead of an income tax, Iowa had imposed a more burdensome gross-receipts tax on the gross receipts from sales to Iowa customers. In *Standard Pressed Steel Co. v. Washington Revenue Dept.,* 419 U.S. 560, 95 S. Ct. 706, 42 L. Ed. 2d 719, the Court sustained a tax on the entire gross receipts from sales made by the taxpayer into Washington State. Because receipts from sales made to States other than Washington were not included in Standard Pressed Steel's taxable gross receipts, the Court concluded that the tax was " 'apportioned exactly to the activities taxed.' " *Id.,* at 564.

437 U.S. at 280. This very point was recently reiterated by this Court in *Tyler Pipe Industries, Inc. v. Washington State Department of Revenue,* ____ U.S. ____, 107 S. Ct. 2810, 2822 (1987).

Moreover, the apportionment method adopted by Illinois need not eliminate all possibilities of multiple taxation.[7] In *Moorman Mfg.,* plaintiff argued that because other states used a three factor formula, and Iowa used only a sales factor, the Iowa tax was unfairly apportioned and would lead to multiple taxation. This Court rejected these arguments and recognized perfect apportionment was not required. *Id.* at 278.

Thus, even when the Illinois tax is viewed as one imposed directly on interstate telephone calls, it is fairly apportioned because it chooses sales, an accepted factor, to apportion its tax on the universe of all telephone calls subject to taxation. Apportionment formulas based on sales have been consistently upheld by this Court, and the Act requires no different ruling.

[7] The only type of tax which could conceivably satisfy Appellants would be a tax apportioned on a call by call basis. This is not required. In *Container Corp. of America v. Franchise Tax Board,* 463 U.S. 159, 181-84, *reh'g denied,* 464 U.S. 909 (1983), this Court held that such detailed transactional accounting is not necessary to pass the apportionment test.

CONCLUSION

The Act imposes a traditional tax on activity which occurs within Illinois. The decision of the Illinois Supreme Court upholding the constitutionality of the Act properly applied the precedents of this Court. There is no need for further argument. The decision of the Illinois Supreme Court should be affirmed.

Respectfully submitted,

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(2)

No. 87-1101

In The

Supreme Court of the United States

October Term, 1987

GTE SPRINT COMMUNICATIONS
CORPORATION,

Appellant,

v.

ROGER D. SWEET, Director of
the Illinois Department of Revenue,
and JEROME COSENTINO, Treasurer
of the State of Illinois,

Appellees.

On Appeal from the
Supreme Court of Illinois

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I. The Act Does Not Tax Local Activity

The State vigorously argues that the taxable event under the Tax Act is purely local in nature. But the Illinois Supreme Court has already held that the taxable activity is not local but interstate calling—and this Court should defer to that construction. Goldberg Jurisdictional Statement at 8a-9a (hereafter "Goldberg Statement").

Even without such deference, the tax should be construed as one on interstate calling. The Tax Act clearly states that a 'tax is imposed upon the act or privilege of originating or receiving interstate telecommunications,' which activity depends upon and is inextricably bound to interstate transmission. Thus, the Illinois tax on the privilege of engaging in the instate portion of interstate communication, like the taxes in *American Trucking* on the privilege of using instate roads necessary for interstate travel, is a tax on interstate activity and must pass the Commerce Clause tests. *American Trucking Associations, Inc. v. Scheiner*, 107 S. Ct. 2829 (1987); GTE Sprint Jurisdictional Statement at 8-10 (hereafter "GTE Sprint Statement").

The State's contortion of the language and practical meaning of the Tax Act does not change this result. For example, although the State argues that the origination and receipt of a long distance call is "local" activity, this Court in *Michigan-Wisconsin Pipe Line Co. v. Calvert*, 347 U.S. 157 (1954) stated that a tax laid on the supposedly "local" loading and unloading of gas onto and off an interstate pipeline constituted a tax on interstate activity. The Court struck down the tax on the full value of the gas transmission because the "local" origination/termination was, as here, an inherent part of interstate transmission. The State also argues that, because the tax is applied to long distance calls which are charged to an Illinois service address (though they may be billed/paid for elsewhere), the tax is effectively a tax on local "sales" activity. But, in *Central Greyhound Lines, Inc. v. Mealey*, 334 U.S. 653 (1948), previously discussed, a tax applied to ticket sales for interstate bus trips (which began and ended in the taxing state) was construed as taxing interstate

activity, although the taxed services were all purchased within the taxing state. GTE Sprint Statement at 9, n.5.[1] In sum, all applicable precedent supports the Illinois Supreme Court's construction of the statute. The State's arguments should therefore be rejected.[2]

II. The Tax Is in No Way Apportioned to the Illinois Portion of the Taxed Interstate Calling Activity

A tax on interstate activity must be apportioned, but, as already shown, the Illinois tax is not. In response, the State makes two arguments. First, the State argues that the tax needs no apportionment (is "100%" apportioned) because the tax taxes purely instate activity. This position must be rejected, for the reasons already stated *supra* at 1-2.

Further, the legal precedents the State cites to pursue its argument that the tax is local are clearly inapplicable. For example, the State cites to *Commonwealth Edison Co. v. Montana*, 453 U.S. 609 (1981) where the Court held an "unapportioned" tax valid. However, the tax there was placed on the distinctly local severance of coal from the land, even though what was mined instate was *later* destined for interstate transportation and out-of-state sale, both divorced from the mining activity itself. State's Motion at 9. Here, participation in the origination/receipt of interstate calls cannot be divorced from interstate transmission, as shown *supra*. The Illinois tax in no way resembles a severance tax.

[1] GTE Sprint has already demonstrated that the tax does not tax calls "purchased at retail" in Illinois, because the tax is assessed against calls even when billed or paid for *outside* Illinois. GTE Sprint Statement at 10.

[2] The State also argues that the Act taxes one person for the entire charge of a call because the telephone company may elect to "divide the charges for telephone services between the originator and recipient" and that, therefore, the tax is somehow a "local tax." State's Motion at 6. There is absolutely nothing in the tax or the record which demonstrates that the phone companies have the discretion, right or practice of so dividing the charges for interstate calls. Such a division would be legally irrelevant, anyhow. *See* discussion *infra* at 6.

The State also cites use and sales tax cases to argue the tax is local and needs no apportionment. But the Tax Act does not resemble such taxes. As to use taxes, the Act does not seek to tax a separable use or consumption instate of a physical item separately and formerly acquired out-of-state. As to a "sales" tax, GTE Sprint has already demonstrated that the Tax Act is applied to calls charged to an Illinois phone, but regardless of whether they are billed or paid for outside the state. Thus, the tax does not even reflect a typical sale made at one instate locale. The "charge" locale of the tax is merely incidental, in any event, and cannot obscure the fact that participation in interstate transmission is not a "local" event, as both courts below recognized. Goldberg Statement at 9a, 21a-22a.[3]

The State also argues, however, that, even assuming the taxable event *is* interstate calling activity, the tax contains sufficient apportionment because it limits itself to long distance calls "sold" in Illinois. State's Motion at 16. Even assuming the tax is limited to calls "sold" in Illinois (which it is not), the tax is still not apportioned. The external consistency test requires that an apportionment formula divide taxable, instate activity from non-taxable, out-of-state activity, along the lines of how the tax base is economically generated. *Container Corporation of America v. Franchise Tax Board*, 463 U.S. 159, 169 (1983). However, the limitation of the tax to calls charged to an Illinois address does not do so.

To illustrate: In *Central Greyhound*, discussed above, New York assessed a sales tax on bus trips beginning and ending in New York, but travelling through New Jersey and Pennsylvania

[3] GTE Sprint has already shown that the tax does not resemble a "complementary" use tax. GTE Sprint Statement at 23-24. Further, this Court has reserved ruling on the question of whether, on out-of-state purchases by a resident, the resident can be taxed by both the outside state on the sale and by the resident state on the use. *Williams v. Vermont*, 472 U.S. 14 (1985). There is thus typically no question of the proper apportionment of use/sales taxes as the Court has yet to reach that issue. There certainly was no such question posed in the *National Geographic* case cited by the State. State's Motion at 9.

as well. The tax was laid on the full purchase price of the trip tickets. The Court struck down the tax despite the fact that *all* ticket sales were made in New York. GTE Sprint Statement at 12, n.6. Clearly, confining the tax to tickets purchased in New York did not limit the tax to that portion of the interstate travel (or costs) attributable to New York. Likewise, the supposed Illinois "charge" apportionment formula in no way adjusts the tax for the differences in the amount of Illinois activity occurring among different interstate phone calls; the tax is be applied to all calls equally.[4] Thus, the "limit" in the Illinois tax is arbitrary and does not apportion it, under *Container*.[5]

III. The Tax Act Discriminates against Interstate Commerce

A. The Facial Equality of the Tax Does Not Negate Its Discriminatory Effect

It does not follow, as the State maintains, that simply because the Tax Act applies a 5% tax to both intra- and interstate calls, the tax does not discriminate. Just last term, this Court struck down such a facially "equal" tax, stating:

> [T]he Commerce Clause has a deeper meaning that may be implicated even though state provisions . . . do not allocate tax burdens between insiders and outsiders in a manner that is facially discriminatory.

American Trucking, 107 S. Ct. at 2839. In *American Trucking*, an equal and flat tax was applied to trucks in both intra- and interstate commerce, for the privilege of utilizing Pennsylvania's

[4] The State cites *Moorman Mfg. Co. v. Bair*, 437 U.S. 267 (1978) to argue that the charge limit in the Illinois tax effects apportionment. In *Moorman*, the single factor sales formula was utilized to divide instate *income* from out-of-state *income*. But *Moorman* in no way supports the use of a single factor sales formula to apportion a tax, not on income, but on interstate calling activity.

[5] The State suggests no better apportionment is possible. State's Motion at 17, n.7. Florida's tax on long distance phone calls beginning or ending in Florida, based on instate transmission mileage, belies the State's argument. GTE Sprint Statement at 13, n.7.

highways. Despite this "equality" of taxing, the Court held that the interstate carriers were bearing a proportionately heavier tax burden than the instate carriers, because the interstate carriers would tend to utilize instate facilities less than the instate carriers:

> Although out-of-state carriers obtain a privilege to use Pennsylvania's highways that is nominally equivalent to that which local carriers receive, imposition of the flat taxes for a privilege that is several times more valuable to a local business than to its out-of-state competitors is unquestionably discriminatory and thus offends the Commerce Clause.

American Trucking, 107 S. Ct. at 2841. Similarly, the "equal" Illinois tax is proportionately higher on interstate calls than on intrastate calls, because interstate calls utilize the instate facilities far less than instate calls do.[6] Thus, the 5%/5% treatment cannot save the Illinois tax.[7]

B. The Tax Fails the Internal Consistency Test

The State argues the tax meets the internal consistency test because "[i]f each, or any, of the other states enacted the tax in question—a tax on a person originating or receiving a call in that state and charging the call to a service address in that state—there would be no discriminatory impact upon interstate commerce." State's Motion at 12. This argument misses the mark.

Specifically, the State's argument assumes that, under the internal consistency test, the Court need only hypothesize that

[6] The Illinois tax is even more insidious than those struck down in *American Trucking* because the *less* Illinois activity is involved in an interstate call, the *more* Illinois taxes it. GTE Sprint Statement at 26. Further, this tendency of the tax to so discriminate is enough to invalidate it. *American Trucking*, 107 S. Ct. at 2842.

[7] The State invokes the *Commonwealth Edison* tax on the severance of coal in Montana to argue the Illinois tax is nondiscriminatory. But, there, the tax was upheld because it was laid on purely local activity, so facial equality between intra- and interstate taxes was not even an issue.

a tax *identical* to the tax at issue is applied in every state, and end its inquiry there. However, in *Armco v. Hardesty*, 467 U.S. 638, 644 (1984), this Court held that the internal consistency test required the application of the same "or *like*" tax in every jurisdiction. This *must* be the test for the following reason: As long as a state tax passes constitutional muster, it must be upheld. As a consequence, if a tax on long distance calls originating/terminating and charged to an Illinois address is deemed constitutional, other states should be permitted to pass taxes on long distance calls which (for example) originate/terminate and are billed or paid for within their borders, because, constitutionally, such taxes are virtually identical to the Illinois tax. But the imposition of both such taxes leads to multiple states taxing, realistically, the same purchase price for the same call. Therefore, the *Armco* internal consistency test must include application of "like" taxes to foreclose semantical end-runs around the internal consistency test. As a consequence, the tax fails this test. GTE Sprint Statement at 15-17.

C. Other States Could Tax the Same or Different Entities on the Same Calls

The State argues that "no other jurisdiction has an adequate basis to tax *the person* who is in Illinois during the telephone call and charges the telephone call to an Illinois address," so the Illinois tax poses no real threat of multiple taxation. State's Motion at 12. This is wrong. Sprint has already submitted uncontested evidence to show that a business may charge a long distance call to a phone in Illinois, but be billed for the call in another office in another state—and that Sprint could assess two different states' taxes on the call on the same bill. GTE Sprint Statement at 16 and n.9. Further, the relevancy of the State's point is questionable, in any event, since this Court long ago held that the pertinent inquiry is whether or not the same *activity* is subject to multiple taxation, regardless of whether one or more persons or entities bear it. *Telegraph Co. v. Texas*, 105 U.S. 460,

465 (1881).[8] Thus, the State's argument collapses upon factual and legal scrutiny.

D. The Credit Provision Does Not Cure the Discriminatory Effect of the Tax

The State finally argues that, in the event Illinois and another state tax the same call, the Tax Act provides a credit in the amount of the other state's tax, so that any threat of multiple taxation is foreclosed. It is not.

First, as previously shown, if the tax applied by the other state does not equal or exceed the Illinois tax, Illinois continues to tax the call along with the other state, but to a lesser degree. GTE Sprint Statement at 22. Under the credit provision, a taxpayer paying a 3% Indiana tax and a 5% Illinois tax on the same call would be required to pay the tax in Indiana, pay the tax in Illinois, receive a credit in Illinois of 3%—all so that its Illinois tax would simply be reduced. The taxpayer would still have paid two taxes on the same call, albeit at a lower rate in Illinois. Further, payment of both taxes constitutes impermissible multiple taxation because the credit reduction in no way operates to divide the tax between Indiana and Illinois, according to what percentage of the calling activity occurred in each state. *See* discussion *supra* at 4-5; GTE Sprint Statement at 22. In addition, even though the credit provision would eradicate the Illinois tax if a tax applied by another state equalled or exceeded the Illinois tax, there is certainly no guarantee this will occur. Therefore, the tax remains discriminatory, despite the credit provision. *Cf. Halliburton Oil Well Cementing Co. v. Reily*, 373 U.S. 64, 76 (1963) (Brennan, J., concurring).

Second, the significant effort required of the interstate callers to obtain the tax credit creates a burden on such callers not borne by instate callers, and effects discrimination. GTE Sprint Statement at 22. The State maintains this does not

[8] The State's citation to *Tyler Pipe* on this point is irrelevant because the Tax Act is not an instate "sales" tax, as is the tax in the example discussed in the *Tyler Pipe* quote.

impose an undue burden, because the Illinois credit provision is identical to use tax credits (for paid sales taxes), "which [credit provisions] have been upheld by this Court." State's Motion at 13. However, this Court has never "upheld" any such credit provisions under Commerce Clause attack. Indeed, this Court has twice reserved for decision the very question of whether use and sales taxes even tax the same activity and, therefore, by implication, whether application of a use tax even requires a credit for a paid sales tax.[9] Even more important, GTE Sprint maintains that the Tax Act simply cannot constitute a "complementary" sales/use tax scheme, because the activity taxed is vastly different. *See* discussion *supra* at 3. Therefore, the existence of unreviewed credit provisions in use taxes is not probative of the legality of their operation with regard to interstate transmission taxes.[10] This Court should therefore find the credit provision inadequate or, at the least, accept review of this unresolved question.[11]

IV. The Illinois Tax Is in No Way Related to Illinois Benefits Accorded the Taxed Activity

GTE Sprint has already shown that the more out-of-state calling activity a long distance call involves, the heavier the

[9] *See* n. 3, *supra*. The states have generally provided use tax credits for paid sales taxes, for fear this Court will hold that the sale and use of a tangible good in two different states represents the same activity. But this Court has not directly ruled on the question. *See Williams v. Vermont*, *supra*; *Henneford v. Silas Mason Co.*, 300 U.S. 577 (1937). The footnote in *Tyler Pipe* the State refers to merely suggests that credit provisions *might* alleviate discrimination which *might* arise under the sales/use tax schemes.

[10] Further, a credit provision in the typical use tax must operate much differently than the credit provision at issue here inasmuch as use taxes are applied to more casual activity than the constant and pervasive activity of interstate calling at issue here.

[11] The State maintains that the ability of the credit provision to save the Illinois tax cannot be reviewed because Sprint has not demonstrated *actual* application of other taxes to the same calling activity taxed by Illinois. State's Motion at 13, n.5. Such a showing is clearly not necessary under *Armco*. *See* GTE Sprint Statement at 15.

Illinois tax becomes. GTE Sprint Statement at 26. The tax is thus absolutely unrelated to the measure of services or benefits the State provides with regard to these calls, and flunks the fourth *Complete Auto* test.

The State's arguments in response are weak. The State, citing *Commonwealth Edison*, implies that the fair relation test is satisfied as long as the taxed activity has some nexus to the taxing state since the state may tax to any degree, on the basis of the 'organized society' benefits it provides to all activities within its border. Just last term, however, this Court rejected the *Commonwealth Edison* emasculation of the fair relation test. In *American Trucking*, the Court held that a flat tax on interstate carriers for the privilege of using Pennsylvania's roads in their interstate travel was unconstitutional, under a much stricter fair relation test:

> [W]hen the measure of a tax bears no relationship to the taxpayers' presence or activities in a State, a court may properly conclude under the fourth prong of the *Complete Auto Transit* test that the State is imposing an undue burden on interstate commerce.
>
> * * *
>
> . . . But a tax levied for the privilege of using roads, and not their actual use, may, in the normal course of operations and not as a fanciful hypothesis, involve an undue burden on interstate carriers. While the privilege extended by a State is . . . theoretically the same for all vehicles, whether interstate or intrastate, the intrastate vehicle can and will exercise the privilege whenever it is in operation, while the interstate vehicle must necessarily forego the privilege some of the time simply because of its interstate character, *i.e.*, because it operates in other states as well. In the general average of instances, the privilege is not as valuable to the interstate as to the intrastate carrier.

American Trucking, 107 S. Ct. at 2844 (citations omitted). Likewise, here, the privilege Illinois accords interstate—versus intrastate—callers is worth significantly *less* because intrastate callers use Illinois facilities more than interstate callers do. Under *American Trucking*, the Illinois tax fails. *See* n.6 *supra*.

The State also argues that the tax is 'fairly related' because it does not impose a tax on a party outside Illinois. The State is simply wrong. Although a call may be charged to equipment in Illinois and involve a caller in Illinois, it is possible that the tax may be billed to or paid for by a party outside Illinois, as the multi-state business example demonstrates. *See* discussion *supra* at 6. Furthermore, simply imposing the tax on an Illinois resident does not fairly relate the Illinois tax to that portion of the interstate transmission activity which occurs in Illinois.

Finally, the State claims the tax is 'fairly related' because it is "based on the value the person in Illinois places upon [the taxed] activity measured by the amount he is *willing* to pay for a telephone call." State's Motion at 15-16 (emphasis added). This argument is nonsensical. Nothing in the record supports such a statement, and it defies common sense to state that the consumer decides how much he wishes to pay the carrier for the carrier's services. The State's fair relation argument is thus easily dismissed, and the tax deserves invalidation by this Court, pursuant to *American Trucking*.

V. Conclusion

For the reasons stated above, GTE Sprint respectfully requests that this Court note probable jurisdiction and reverse the decision of the Illinois Supreme Court.

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(5) (4)

Nos. 87-826, 87-1101

Supreme Court, U.S.
FILED
APR 29 1988
JOSEPH F. SPANIOL, JR.
CLERK

In The Supreme Court of the United States

October Term, 1987

JEROME F. GOLDBERG, ROBERT McTIGUE
and GTE SPRINT COMMUNICATIONS CORPORATION,
Appellants,

v.

ROGER D. SWEET, Director of the Illinois
Department of Revenue, and JEROME COSENTINO,
Treasurer of the State of Illinois,
Appellees.

On Appeal from the
Supreme Court of Illinois

JOINT APPENDIX

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Appeals Docketed November 20, 1987 and December 31, 1987
Probable Jurisdiction Noted February 22, 1988

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CHRONOLOGICAL LIST OF RELEVANT DOCKET ENTRIES

Circuit Court of Cook County, Illinois

Aug. 13, 1985 – Plaintiffs' class action complaint for declaratory judgment, injunctive relief, accounting and other relief filed in Circuit Court of Cook County, Illinois, Chancery Division, alleging that the Illinois Telecommunications Excise Tax Act ("Illinois Tax Act") is unconstitutional under the Illinois and U.S. Constitutions.

Sept. 24, 1985 – Answer of defendant Electronic Office Centers of America filed.

Sept. 27, 1985 – Answer of defendant J. Thomas Johnson, Director of the Illinois Department of Revenue, filed.

Sept. 27, 1985 – Answer of defendant Allnet Communications Services, Inc. filed.

Oct. 7, 1985 – Motion to dismiss of defendant Satellite Business Systems filed.

Oct. 8, 1985 – Answer and verified counterclaim (cross-claim) of defendant GTE Sprint Communications Corporation for injunctive, declaratory and other relief filed, the counterclaim (cross-claim) alleging that the Illinois Tax Act is unconstitutional under the Commerce Clause of the U.S. Constitution.

Oct. 9, 1985 – Stipulation between GTE Sprint Communications Corporation and the Illinois Department of Revenue and the Illinois State Treasurer agreeing to entry of an order for maintenance of GTE Sprint Communications Corporation's tax payments under the Illinois Tax Act, and those of its customers, in protest fund.

Oct. 29, 1985 – Agreed order for injunction between GTE Sprint Communications Corporation and Illinois Department of Revenue and Illinois State Treasurer entered, ordering that tax payments by GTE Sprint and its customers under the Illinois Tax Act are to be maintained

in the protest fund, pursuant to the Money Disposition Act, pending final resolution of the lawsuit.

Nov. 8, 1985 – Answer of defendant TDX Systems, Inc. filed.

Nov. 12, 1985 – Answer and verified counterclaim of defendant MCI Telecommunications Corporation for injunctive, declaratory and other relief filed.

Nov. 12, 1985 – Answer of defendant American Telephone and Telegraph Company filed.

Nov. 14, 1985 – Emergency motion for temporary restraining order or preliminary injunction filed by defendant and counter-plaintiff MCI Telecommunications Corporation.

Nov. 14, 1985 – Order for preliminary injunction entered ordering that tax payments by MCI Communications Corporation and its customers are to be maintained in the protest fund, pending final resolution of the lawsuit.

Nov. 14, 1985 – Order entered extending injunction to tax payments made by U.S. Telecommunications and Republic Telecommunications and their customers.

Nov. 22, 1985 – Plaintiffs' motion to join Illinois Bell Telephone Company as a defendant filed.

Nov. 22, 1985 – Plaintiffs' emergency motion for preliminary injunction and creation of a special escrow fund or, in the alternative, for an order that tax payments under the Illinois Tax Act be deemed made under protest, filed.

Nov. 22, 1985 – Response of defendants Department of Revenue and Illinois State Treasurer to plaintiffs' emergency motion for preliminary injunction and creation of a special escrow fund or, in the alternative, for an order that tax payments under the Illinois Tax Act be deemed made under protest, filed.

Nov. 22, 1985 – Verified answer of counter-defendants Illinois Department of Revenue and Illinois State Treasurer to verified counterclaim of defendant and counter-plaintiff GTE Sprint Communications Corporation filed.

Nov. 27, 1985 – Intervening petition of Ruppman Marketing Services, Inc. filed.

Nov. 27, 1985 – Class action complaint of intervenor Ruppman Marketing Services, Inc. for declaratory judgment, injunctive relief, accounting and other relief filed.

Dec. 9, 1985 – Emergency motion of counter-plaintiff Satellite Business Systems for a temporary restraining order or preliminary injunction filed.

Dec. 9, 1985 – Answer and verified counterclaim of defendant Satellite Business Systems for injunctive, declaratory and other relief filed.

Dec. 12, 1985 – Illinois Department of Revenue and Illinois State Treasurer's memorandum of law in support of their response to plaintiffs' emergency motion for preliminary injunction and creation of a special escrow fund filed.

Dec. 12, 1985 – Agreed order for preliminary injunction between plaintiffs Jerome F. Goldberg and Robert McTigue and defendants Illinois Department of Revenue and Illinois State Treasurer and defendant American Telephone and Telegraph Company entered, ordering that tax payments by AT&T and its customers are to be maintained in the protest fund, pending final resolution of the lawsuit.

Dec. 13, 1985 – Answer of defendant Illinois Bell Telephone Company filed.

Dec. 18, 1985 – Objections of counter-defendants Illinois Department of Revenue and Illinois State Treasurer to the intervening petition of Ruppman Marketing Services, Inc. filed.

Dec. 20, 1985 – Order for preliminary injunction entered, ordering that tax payments by Satellite Business Systems and its customers are to be maintained in the

protest fund, pending final resolution of the lawsuit.

Dec. 20, 1985 – Order for preliminary injunction entered, ordering that tax payments by American Telephone and Telegraph Company and its customers are to be maintained in the protest fund, pending final resolution of the lawsuit.

Dec. 30, 1985 – Plaintiffs' motion for class certification filed.

Dec. 30, 1985 – Memorandum of law of defendant and counter-plaintiff GTE Sprint Communications Corporation in support of plaintiffs' motion for preliminary injunction filed.

Dec. 30, 1985 – Plaintiffs' reply memorandum in support of their emergency motion for preliminary injunction and creation of a special escrow fund filed.

Jan. 2, 1986 – Response to objections of Illinois Department of Revenue and Illinois State Treasurer to the intervening petition of Ruppman Marketing Services, Inc. filed.

Jan. 10, 1986 – Verified answer of counter-defendants Illinois Department of Revenue and Illinois State Treasurer to verified counterclaim of MCI Telecommunications Corporation filed.

Jan. 10, 1986 – Plaintiffs' response to intervening petition of Ruppman Marketing Services, Inc. filed.

Jan. 10, 1986 – Order of preliminary injunction entered requiring defendants GTE Sprint, Satellite Business Systems, Western Union, Max Long Distance, TMC Long Distance, TDX Systems, Inc., MCI Telecommunications Corp., Inc., ITT, Allnet Dial One Service, Republic Telecom Corp., U.S. Telecom, AT&T, Illinois Bell Telephone Company, and Electronic Office Centers of America, Inc. to remit under protest to the Illinois Department of Revenue all taxes collected by the carriers from their customers pursuant to the Illinois Telecommunications Excise Tax Act, all such tax payments to be placed by the Illinois

Department of Revenue into a special protest fund, to be preserved pending final resolution of the lawsuit.

Jan. 10, 1986 – Order entered denying the intervening petition of Ruppman Marketing Services, Inc.

Feb. 4, 1986 – Response of defendants Illinois Department of Revenue and Illinois State Treasurer in opposition to plaintiffs' motion for class certification filed.

Feb. 26, 1986 – Plaintiffs' reply memorandum in support of motion for class certification filed.

Mar. 4, 1986 – Verified answer of Illinois Department of Revenue and Illinois State Treasurer to the verified counterclaim of Satellite Business Systems for injunctive, declaratory and other relief filed.

Mar. 4, 1986 – Order of preliminary injunction entered requiring defendants GTE Sprint, Satellite Business Systems, Western Union, Max Long Distance, TMC Long Distance, TDX Systems, Inc., MCI Telecommunications Corp., ITT, Allnet Dial One Service, Republic Telecom Corp., U.S. Telecom, AT&T, Electronic Office Centers of America, Inc. and Illinois Bell Telephone Company to remit under protest all taxes collected by the carriers from their customers pursuant to the Illinois Telecommunications Excise Tax Act, all such tax payments to be placed by the Illinois Department of Revenue into a special protest fund, to be preserved pending final resolution of the lawsuit.

Apr. 14, 1986 – Order entered denying class certification.

May 2, 1986 – Motion of counter-defendants Illinois Department of Revenue and Illinois State Treasurer for summary judgment against plaintiffs Goldberg and McTigue and defendant-counter-plaintiff MCI Telecommunications and for partial summary judgment against defendant-counter-plaintiffs GTE Sprint and SBS Skyline filed.

May 23, 1986 – Answer of defendant Republic Telecom Services Corporation filed.

May 23, 1986 – Answer of defendant U.S. Telecommunications Services Company filed.

June 9, 1986 – Memorandum of law in support of defendants-counter-defendants Illinois Department of Revenue and Illinois State Treasurer's motion for summary judgment and for partial summary judgment filed.

July 25, 1986 – Motion of defendant-counter-plaintiff GTE Sprint Communications Corporation for partial summary judgment filed.

July 28, 1986 – Memorandum of law in support of plaintiffs' motion for summary judgment and in opposition to defendants-counter-defendants Illinois Department of Revenue and Illinois State Treasurer's motion for summary judgment filed.

July 28, 1986 – Memorandum of law in support of motion of defendant-counter-plaintiff GTE Sprint Communications Corporation for partial summary judgment filed.

Aug. 11, 1986 – Memorandum of law of defendant-counter-defendant Illinois Department of Revenue in opposition to plaintiffs' and counter-plaintiff's motions for summary judgment filed.

Aug. 25, 1986 – Reply memorandum in support of plaintiffs' motion for summary judgment filed.

Aug. 26, 1986 – Counter-plaintiff GTE Sprint Communications Corporation's memorandum in reply to defendant-counter-defendant Illinois Department of Revenue's memorandum in opposition to its motion for partial summary judgment filed.

Sept. 24, 1986 – Plaintiffs' renewed motion for class certification filed.

Sept. 25, 1986 – Response of defendants Illinois Department of Revenue and Illinois State Treasurer in

opposition to plaintiffs' renewed motion for class certification filed.

Sept. 27, 1986 – Answer of defendant Lexitel Corporation filed.

Oct. 1, 1986 – Plaintiffs' reply memorandum of law in support of their renewed motion for class certification filed.

Oct. 6, 1986 – Defendant Illinois Bell Telephone Company's motion for declaration of rights filed.

Oct. 20, 1986 – Original transcripts of proceedings before Judge Richard L. Curry in the Circuit Court of Cook County, Illinois, Chancery Division, on Jan. 6, 1986, Jan. 10, 1986, Mar. 4, 1986, May 2, 1986, Sept. 16, 1986, Sept. 25, 1986 and Oct. 6, 1986 filed.

Oct. 22, 1986 – Order entered declaring the Illinois Telecommunications Excise Tax Act unconstitutional under the Illinois and U.S. Constitutions and therefore granting plaintiffs' motion for summary judgment; granting defendant-counter-plaintiff GTE Sprint Communications Corporation's motion for partial summary judgment; and denying defendant-counter-defendants Illinois Department of Revenue and Illinois State Treasurer's motion for summary judgment against plaintiffs and counter-plaintiff MCI Telecommunications and for partial summary judgment against counter-plaintiffs GTE Sprint and SBS Skyline. Order also denies plaintiffs' renewed motion for class certification; grants defendants Illinois Department of Revenue and Illinois State Treasurer's motion to stay effectiveness of order pending appeal; and grants motion for declaration of rights by defendant Illinois Bell Telephone Company regarding obligations under certain provisions of the Illinois Tax Act.

Supreme Court of Illinois

Nov. 6, 1986 – Notice of direct appeal to Illinois Supreme Court from Circuit Court's Order of October 22, 1986 declaring Illinois Tax Act unconstitutional, filed by

defendants Illinois Department of Revenue and Illinois State Treasurer.

Dec. 15, 1986 – Plaintiffs' notice of cross-appeal filed.

Dec. 16, 1986 – Order entered granting GTE Sprint Communications Corporation's motion to correct docketing statement and caption.

Feb. 13, 1987 – Brief of appellant Illinois Department of Revenue filed.

Apr. 2, 1987 – Brief of plaintiffs-appellees-cross-appellants Jerome F. Goldberg and Robert McTigue filed.

Apr. 2, 1987 – Responsive brief of counter-plaintiff-appellee GTE Sprint Communications Corporation filed.

Apr. 16, 1987 – Reply brief of defendant-appellant Illinois Department of Revenue filed.

Apr. 21, 1987 – Brief of *amicus curiae* National Tax Payers Union in support of plaintiffs-appellees filed.

May 4, 1987 – Reply brief of plaintiffs-appellees-cross-appellants in support of their cross-appeal filed.

May 28, 1987 – Brief of *amicus curiae* Illinois Municipal League filed.

June 24, 1987 – Order of the Illinois Supreme Court entered, with opinion forthcoming, holding the Illinois Telecommunications Excise Tax Act constitutional and reversing the judgment of the Circuit Court of Cook County, Illinois that the Illinois Tax Act is unconstitutional.

July 15, 1987 – Petition for rehearing of defendant-cross-plaintiff-appellee GTE Sprint Communications Corporation filed with the Illinois Supreme Court.

July 15, 1987 – Motion of defendants-appellants Illinois Department of Revenue and Illinois State Treasurer for entry of an order releasing tax payments held in protest fund.

July 20, 1987 – Defendant-cross-plaintiff-appellee GTE Sprint Communications Corporation's objection to motion for entry of an order authorizing release of tax payments and motion for a stay filed.

July 21, 1987 – Plaintiffs-appellees' objections to defendants-appellants' motion for release of tax payments and motion for appropriate relief filed.

July 27, 1987 – Opinion of Illinois Supreme Court holding Illinois Telecommunications Excise Tax Act constitutional under the Illinois and U.S. Constitutions issued.

July 31, 1987 – Reply of defendants-appellants Illinois Department of Revenue and Illinois State Treasurer in further support of their motion for entry of order releasing tax payments and in opposition to plaintiffs-appellees' motion for appropriate relief filed.

Aug. 17, 1987 – Plaintiffs-appellees' memorandum in support of their objections to defendants-appellants' motion for release of tax payments from protest fund and in support of their motion for appropriate relief filed.

Aug. 17, 1987 – Joint motion and stipulation between defendant-cross-plaintiff-appellee GTE Sprint Communications Corporation and defendant-appellant Illinois Department of Revenue filed, the stipulation agreeing to the withdrawal of GTE Sprint's previously-filed objections and to the substitution of new objections by GTE Sprint to the release of GTE Sprint's or its customers' tax payments or any other payments for which GTE Sprint might be deemed liable.

Aug. 24, 1987 – Defendants-appellants Illinois Department of Revenue and Illinois State Treasurer's objections to plaintiffs-appellees' motion for stay of mandate filed.

Aug. 28, 1987 – Order entered by Illinois Supreme Court, authorizing Illinois State Treasurer to transfer from the protest fund to the general revenue fund of the State of Illinois those tax payments made under the Illinois Tele-

communications Excise Tax Act by AT&T, MCI and Illinois Bell, or their customers, by agreement of AT&T, MCI and Illinois Bell.

Aug. 28, 1987 – Order entered allowing the joint motion and stipulation (filed Aug. 17, 1987) between defendant-cross-plaintiff-appellee GTE Sprint and defendant-appellant Illinois Department of Revenue, and allowing the motion for stay of mandate pending appeal to the United States Supreme Court.

Oct. 5, 1987 – Order entered denying petition for rehearing of defendant-cross-plaintiff-appellee GTE Sprint Communications Corporation.

Supreme Court of the United States

Oct. 26, 1987 – Notice of appeal of plaintiffs-appellees Jerome F. Goldberg and Robert McTigue to the Supreme Court of the United States filed.

Nov. 20, 1987 – Appellants Goldberg and McTigue docket appeal.

Dec. 7, 1987 – Notice of appeal of defendant-cross-plaintiff-appellee GTE Sprint Communications Corporation to the Supreme Court of the United States filed.

Dec. 31, 1987 – Appellant GTE Sprint dockets appeal.

Jan. 29, 1988 – Appellees' Consolidated Motion To Affirm filed.

Feb. 9, 1988 – Appellant GTE Sprint's Brief in Reply to Consolidated Motion To Affirm filed.

Feb. 10, 1988 – Appellants Goldberg and McTigue's Brief in Opposition to Motion To Affirm filed.

Feb. 22, 1988 – Order of the United States Supreme Court, noting probable jurisdiction on appeals of Goldberg, McTigue and GTE Sprint Communications Corporation, and consolidating appeals for review.

LIST OF RECORD ENTRIES AND STATUTES ALREADY INCLUDED IN APPENDICES TO JURISDICTIONAL STATEMENTS

The following opinions, decisions, judgments, orders and statutes have been omitted in printing this Joint Appendix because they appear on the following pages in either the Appendix to the printed Jurisdictional Statement in *Goldberg, et al. v. Sweet, et al.*, No. 87-826 ("Goldberg J.S. App.") or in the Appendix to the printed Jurisdictional Statement in *GTE Sprint Communications Corporation v. Sweet, et al.*, No. 87-1101 ("Sprint J.S. App."), as follows:

	Page
Illinois Telecommunications Excise Tax Act, effective August 1, 1985	Goldberg J.S. App. 25a
Affidavit of Richard N. Wiley, dated July 25, 1986	Sprint J.S. App. 7a
Order and Findings and Conclusions of the Circuit Court of Cook County, County Department, Chancery Division, dated October 21, 1986	Goldberg J.S. App. 18a
Order of the Illinois Supreme Court, filed June 24, 1987	Goldberg J.S. App. 17a
Opinion of the Illinois Supreme Court, dated July 27, 1987	Goldberg J.S. App. 4a
Denial of the Petition for Rehearing (filed by GTE Sprint Communications Corporation) by the Illinois Supreme Court, dated October 5, 1987	Goldberg J.S. App. 3a; Sprint J.S. App. 6a

No. 87-1101

In The
Supreme Court of the United States

October Term, 1987

GTE SPRINT COMMUNICATIONS CORPORATION,

Appellant,

v.

ROGER D. SWEET, Director of the Illinois Department of Revenue, and JEROME COSENTINO, Treasurer of the State of Illinois,

Appellees.

ON APPEAL FROM THE SUPREME COURT OF ILLINOIS

[ORDER NOTING PROBABLE JURISDICTION]
Filed February 22, 1988

APPEAL from the Supreme Court of Illinois.

The statement of jurisdiction in this case having been submitted and considered by the Court, in this Court, probable jurisdiction is noted. This case is consolidated with 87-826, *Jerome F. Goldberg and Robert McTigue* v. *Roger D. Sweet, Director, Illinois Department of Revenue, et al.*, and a total of one hour is allotted for oral argument.

(6) (5)

Nos. 87-826, 87-1101

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

JEROME F. GOLDBERG AND ROBERT MCTIGUE,
Appellants,
v.

ROGER D. SWEET, DIRECTOR OF THE ILLINOIS DEPARTMENT OF REVENUE, *et al.*,
Appellees.

GTE SPRINT COMMUNICATIONS CORPORATION,
Appellant,
v.

ROGER D. SWEET, DIRECTOR OF THE ILLINOIS DEPARTMENT OF REVENUE, *et al.*,
Appellees.

On Appeal from the Supreme Court of Illinois

BRIEF FOR APPELLANTS GOLDBERG AND McTIGUE

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QUESTION PRESENTED

May a State, consistent with the Commerce Clause, impose a tax on interstate telecommunications that is completely unapportioned, that subjects the telecommunications to multiple state taxation, that increases as the State's contact with the telecommunications decreases, and that lays a heavier burden on interstate telecommunications than intrastate telecommunications?

PARTIES TO THE PROCEEDINGS

Appellants Jerome F. Goldberg and Robert McTigue, plaintiffs before the Cook County Circuit Court and appellees before the Illinois Supreme Court, are residents of Illinois subject to the challenged state tax. Appellee Roger D. Sweet succeeded defendant J. Thomas Johnson as Director of the Illinois Department of Revenue. Appellee Jerry Cosentino succeeded defendant James H. Donnewald as Treasurer of the State of Illinois.

The following telecommunications companies were also named as defendants in the complaint: GTE Sprint Communications Corporation ("GTE Sprint"), MCI Telecommunications Corporation ("MCI"), Satellite Business Systems ("SBS"), Republic Telecom Corporation, U.S. Telecom Communications Services Company, American Telephone and Telegraph Company, Allnet Communications Services, Inc., Electronic Office Centers of America, Inc., Lexitel Corporation, Illinois Bell Telephone Company, International Telephone and Telegraph Corporation, TDX Systems, Inc., TMC Long Distance, and Western Union. GTE Sprint, MCI, and SBS filed counterclaims alleging that the tax at issue was unconstitutional; GTE Sprint also participated as an appellee before the Illinois Supreme Court.

GTE Sprint filed a separate notice of appeal to this Court, and a separate jurisdictional statement (No. 87-1101). This Court noted probable jurisdiction over both appeals, and consolidated them. 108 S. Ct. 1010 (1988).

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

Nos. 87-826, 87-1101

JEROME F. GOLDBERG AND ROBERT MCTIGUE,
Appellants,
v.

ROGER D. SWEET, DIRECTOR OF THE ILLINOIS DEPARTMENT OF REVENUE, *et al.*,
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GTE SPRINT COMMUNICATIONS CORPORATION,
Appellant,
v.

ROGER D. SWEET, DIRECTOR OF THE ILLINOIS DEPARTMENT OF REVENUE, *et al.*,
Appellees.

On Appeal from the Supreme Court of Illinois

BRIEF FOR APPELLANTS GOLDBERG AND McTIGUE

OPINIONS BELOW

The opinion of the Supreme Court of Illinois is reported at 117 Ill.2d 493, 512 N.E.2d 1262, and is reprinted in the appendix to the Goldberg Jurisdictional Statement ("GA") at 4a.

The findings of fact and conclusions of law of the Circuit Court of Cook County (Curry, J.) are unreported and are reprinted at GA 20a.

JURISDICTION

Appellants Goldberg and McTigue filed suit against state officials and various long distance telephone carriers in the Circuit Court of Cook County, Illinois on August 13, 1985, contending that the Telecommunications Excise Tax Act, Ill. Rev. Stat. ch. 120, ¶¶ 2001-2021, contravened, *inter alia,* the Commerce Clause of the United States Constitution, U.S. Const. Art. I, § 8, cl. 3, as well as the Due Process and Equal Protection Clauses. On October 8, 1985, defendant GTE Sprint Communications Corporation ("GTE Sprint") filed a cross-claim against the Director of Revenue, also alleging that the Act was unconstitutional under the Commerce Clause. On October 21, 1986, the Circuit Court (Curry, J.) granted motions for summary judgment in favor of appellants, ruling that the Act violated both the Commerce Clause and Equal Protection Clause of the United States Constitution. GA 18a-24a. The Director of Revenue appealed, and on June 24, 1987, the Illinois Supreme Court issued an order reversing the Circuit Court. GA 17a. On July 27, 1987, the Illinois Supreme Court issued a *per curiam* opinion with respect to its order, GA 4a, and on October 5, 1987, denied a timely-filed petition for rehearing. GA 3a. On October 26, 1987, the Goldberg appellants filed their notice of appeal with the Illinois Supreme Court, GA 1a, and on December 8, 1987, GTE Sprint filed its notice of appeal. *See* GTE Sprint Jurisdictional Statement Appendix ("GTE A") 1a. On February 22, 1988, this Court noted probable jurisdiction and consolidated the Goldberg appeal (No. 87-826) and GTE Sprint appeal (No. 87-1101). Pursuant to a request by GTE Sprint, the time for filing the briefs for appellants was extended to and including April 29, 1988. The jurisdiction of this Court over the appeals rests on 28 U.S.C. § 1257(2).

PERTINENT CONSTITUTIONAL AND STATUTORY PROVISIONS

The Commerce Clause of the United States Constitution, Art. I, § 8, cl. 3, provides in pertinent part that "The Congress shall have Power * * * to regulate Commerce * * * among the several States * * *."

The full text of the Telecommunications Excise Tax Act, Ill. Rev. Stat. ch. 120, ¶¶ 2001-2021, is set forth at GA 25a-47a.

STATEMENT OF THE CASE

Section four of the Illinois Telecommunications Excise Tax Act ("the Act") took effect on August 1, 1985, and imposed a tax "upon the act or privilege of originating in this State or receiving in this State interstate telecommunications * * *." Ill. Rev. Stat. ch. 120, ¶ 2004; GA 29a. The tax is assessed at a flat rate of five percent "of the gross charge for such telecommunications purchased at retail," *id.*, and applies to all calls charged to an Illinois service address, regardless of where the calls are billed or paid. *Id.*, ¶ 2002(a), (b); GA 25a, 26a. The retailer of the calls is required to collect the tax from the person who is charged for the call, and the amount "required to be collected * * * constitute[s] a debt owed by the retailer to [the] State." *Id.*, ¶ 2005; GA 30a.[1] The Act further provides that, "whenever possible," the tax is to be stated as a separate item from the gross charge for telecommunications. *Id.*

In addition to the five percent tax on interstate telecommunications, the Act also imposes a tax on intrastate telecommunications, again at a flat rate of five percent of the gross retail charge. *Id.*, ¶ 2003; GA 29a. Thus, a call that is placed, transmitted, and received entirely in

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[1] Hence, because GTE Sprint failed to set up its billing system by the effective date of the Act so as to be able to collect the tax from its customers, GTE Sprint itself was required to pay some $400,000 in taxes due under the Act. GTE A 10a.

Illinois is taxed at five percent. Similarly, a call placed and charged in Illinois that is transmitted outside Illinois and received in Indiana is still taxed at five percent of the cost of the entire call. If the call is placed to Hawaii, or received in Illinois collect from Hawaii, Illinois again taxes five percent of the total cost of the call.

The section of the Act taxing interstate calls contains a "credit" provision, the stated purpose of which is "[t]o prevent actual multi-state taxation." *Id.*, ¶ 2004; GA 29a. The provision "allow[s]" an Illinois taxpayer a credit against the five percent charge paid to Illinois, provided he proves that he paid another State a tax on the same "event" taxed by Illinois, and that the other State's tax was "properly due." The statute contains no procedures for actually obtaining such a "credit," nor any standards for the requisite proof that the tax paid to the other State was in fact "properly due" and that the other State's tax was imposed on the same "event" taxed by Illinois.

Appellants Jerome F. Goldberg and Robert McTigue, Illinois residents who are subject to and have paid Illinois' five percent tax on interstate telecommunications, filed a class action complaint on August 13, 1985, in Cook County Circuit Court, naming as defendants the Director of the Illinois Department of Revenue and various long-distance telephone carriers (including GTE Sprint) tasked with collecting the tax. The complaint sought a declaration that section four of the Act violated, *inter alia*, the Commerce Clause, the Due Process Clause, and the Equal Protection Clause of the United States Constitution. Goldberg and McTigue also sought an injunction against continued collection of the tax, and an accounting and refund of taxes already collected in violation of the Constitution.

Several of the long-distance carriers (including GTE Sprint) responded by filing cross-claims of their own (denominated "counterclaims") against the Director,

likewise seeking a declaration that the tax on interstate telecommunications was unconstitutional. Appellants thereafter obtained orders, pursuant to Illinois law,[2] requiring that all monies collected in the State by all defendant long-distance carriers be remitted under protest and retained in a special fund. At the time judgment was entered by the court below, there were over 142 million dollars in the protest fund,[3] and payments have continued to be made into it at the rate of approximately ten million dollars per month.

Acting upon cross-motions for summary judgment, the Circuit Court concluded that section four was unconstitutional. In reaching that conclusion, the court first rejected the State's argument that the tax did not implicate the Commerce Clause because it was imposed only on a local purchase or sale. Specifically, the court held

[2] The State Officers and Employees Money Disposition Act, Ill. Rev. Stat. ch. 127, ¶ 172.

[3] Six days after the Illinois Supreme Court entered the judgment subject to appeal in this case, the Illinois General Assembly passed Public Act 85-14, authorizing the State Treasurer to transfer monies from the protest fund to the State's General Revenue Fund, citing the instant lawsuit by name, and providing that "[i]f a final nonappealable order of a court of competent jurisdiction declares [the Act being challenged in this case] void or unconstitutional, the General Assembly shall appropriate" sufficient funds to restore the monies taken from the protest fund created in this case. The repayment provisions relate only to the case at bar. Over the objection of the Goldberg appellants, the Illinois Supreme Court issued an order on August 27, 1987, allowing the Treasurer to transfer some 117 million dollars out of the protest fund, and furthermore allowing transfer of all payments thereafter made into the fund by MCI, AT&T, and Illinois Bell Telephone Company (all of which had agreed to this procedure). GTE Sprint had originally objected to the constitutionality of Public Act 85-14 and the State's motion to withdraw monies from the protest fund, but withdrew its objection in exchange for an agreement that during the pendency of this litigation the State would not seek to withdraw from the protest fund any monies conveyed into it by GTE Sprint.

that the words of the statute "unmistakably mean that the taxable transaction is the interstate phone call" and that "it strains both common knowledge and common sense to characterize an interstate phone call in terms of an Illinois sale at retail and thereby ignore the realities of its interstate participant and the interstate communication system over which it has taken place." GA 20a-21a. The court concluded that the mere fact that the call is charged to an address in Illinois "cannot serve to make local that which is unmistakenly interstate." GA 22a. The court reasoned that the fact that the Legislature had laid its tax on the gross charge for the entire call "makes it clear that the call itself and not its billing in Illinois is what is really being taxed and that event is an interstate activity." GA 21a.

Having determined that Illinois intended to tax interstate commerce, the court then tested the tax by the standards set by this Court. It concluded that the Illinois tax on interstate telecommunications "fails to meet at least three of the four criteria set out in the Supreme Court decision of *Complete Auto* v. *Brady*, 430 U.S. 274." GA 22a. The court held:

> Illinois is attempting to tax the entire cost of an interstate act which takes place only partially in Illinois. This tax by its own terms is not fairly apportioned. It discriminates against interstate commerce and it is not related to services provided in Illinois. [GA 24a.]

"For all these reasons,"[4] the court concluded, "the Act

[4] The Circuit Court also held that the Act violated the Equal Protection Clause, because "it taxes only those who pay for the call and not those whose calls are paid for by others." GA 21a. In addition, the Circuit Court denied a motion by Goldberg and McTigue for class certification. GA 19a. Although it acknowledged that all the prerequisites for class certification were met, the court concluded that a class action was unnecessary because all the monies in dispute were segregated in the protest fund and available for distribution to taxpayers. *See* GA 7a.

must fail." GA 24a.[5]

The state defendants appealed directly to the Illinois Supreme Court. On June 24, 1987, that court issued an order and judgment declaring that the Act was constitutional and reversing the contrary judgment of the Circuit Court. GA 17a. The order stated:

> This announcement is made at this time because of the public importance of this revenue litigation. An opinion setting forth the reasons for the Court's judgment will be completed and filed at a later date. [GA 17a.]

On July 14, 1987, GTE Sprint filed a timely petition for rehearing, urging the Illinois Supreme Court to reconsider its as-yet-unexplained judgment in light of two new decisions of this Court issued the day before that judgment, *American Trucking Associations, Inc.* v. *Scheiner*, 107 S.Ct. 2829, and *Tyler Pipe Industries, Inc.* v. *Washington State Department of Revenue*, 107 S. Ct. 2810.

On July 27, 1987, the four members of the Illinois Supreme Court who participated in the case issued a *per curiam* opinion with respect to the prior judgment. GA 4a. The court began by addressing the State's principal argument on appeal—that section 4 does not tax "the interstate telecommunication itself," but is merely a "retail tax" on the local "purchase of an interstate telecommunication." GA 7a. In rejecting this contention, the court agreed with the Circuit Court that "the fact that section 4 establishes the purchase price of an interstate telecommunication as the basis upon which the tax is calculated does not transform the taxable event into a retail purchase * * *." GA 9a. Instead, the court concluded that

> it is clear that the taxable event is linked inextricably to interstate activity—interstate communication. A person simply cannot make or receive an

[5] The Act provides that "[i]f Section 4 * * * is declared unconstitutional or invalid, no part of this [Act] shall be effective." Ill. Rev. Stat. ch. 120, ¶ 2021; GA 47a.

> interstate telecommunication without activating and participating in a complex network of interstate transmissions culminating in interstate communication. * * * The very process of interstate telecommunication is interstate commerce. [GA 9a.]

Contrary to the Circuit Court, however, the court below held that this state tax on interstate telecommunications did not impermissibly violate any of the three key requirements of *Complete Auto*—that the tax be "fairly apportioned," that it "not discriminate against interstate commerce," and that it be "fairly related to the services provided by the [taxing] State." [6]

In reaching this conclusion, the court acknowledged that the tax "is not an apportioned tax," since it "applies to the entirety of each and every interstate telecommunication." GA 10a. This caused the court to denominate the tax "constitutionally suspect." GA 11a. According to the court below, however, "[i]f the tax avoids the pitfall of multiple taxation, or the risk of such taxation, it is nondiscriminatory; and, the fact that it is unapportioned is not constitutionally significant." GA 11a.

The court held that there could be no danger of such multiple taxation with respect to interstate calls originated in the State because, by definition, "no other taxing entity" could levy a tax on "the origination of an interstate telecommunication in Illinois." GA 11a. With respect to calls received in Illinois, however, the court believed that the Illinois tax *did* present "a real risk of multiple taxation." GA 12a. Indeed, the court noted that the record revealed that at least two jurisdictions outside Illinois already taxed such calls. The court acknowledged that "[c]learly, this is multiple taxation of the same interstate taxable event which would be prohibited by the commerce clause, as interpreted by *Complete Auto* and its

[6] *Complete Auto Transit, Inc.* v. *Brady*, 430 U.S. 274, 279 (1977). There is no dispute that the first prong of the *Complete Auto* test—that the tax be "applied to an activity with a substantial nexus with the taxing state," *id.*—was satisfied in this case.

progeny * * *." GA 12a. The tax was saved from this fate, according to the court below, solely because "section 4 provides a credit against any tax due from a taxpayer who has paid two or more taxes on the same interstate telecommunication." GA 13a.

In light of the foregoing, the court below concluded that the tax was valid even though wholly unapportioned. The court also concluded that the absence of any risk of multiple taxation (because of the credit provision) was sufficient in itself to satisfy the third prong of the *Complete Auto* test—that the tax not discriminate against interstate commerce. GA 13a. The court noted, furthermore, that "the tax does not discriminate in favor of intrastate telecommunications" since "the same 5% levy" is imposed on both interstate and intrastate communications. GA 11a.

Turning finally to the fourth prong of the *Complete Auto* test, the court held that the tax was fairly related to benefits provided by Illinois. The court recognized that "the State is taxing the 'gross charge' of the entire telecommunication even though the benefits it affords are limited to that portion of the communication occurring within the State." GA 13a. The court concluded, nevertheless, that "the benefits afforded by other States in facilitating the same interstate telecommunication are too speculative to override the substantial benefits extended by Illinois." GA 13a. Accordingly, having found that the tax met all the requirements of the Commerce Clause, the Illinois Supreme Court reversed the Circuit Court's decision and sustained the tax.[7]

[7] The court also reversed the Circuit Court's holding that the Act violated the Equal Protection Clause. GA 14a-16a. Although appellants continue to believe that the Circuit Court was correct on this point, we have not sought review of that question by this Court.

In light of the ruling by the court below on the merits, the court vacated as moot the Circuit Court's order denying class certification. GA 16a. No issues regarding class certification are before this Court.

SUMMARY OF ARGUMENT

This Court has long been committed to the proposition that the States may tax interstate commerce and thereby require it to pay its "just share" of the cost of state services. *Complete Auto Transit, Inc.* v. *Brady*, 430 U.S. at 279 (citing *Western Live Stock* v. *Bureau of Revenue*, 303 U.S. 250, 254 (1938)). But the Court has also made clear that if the States do elect to tax interstate commerce, they must assure that it will not pay *more* than its "just share." To provide that assurance, state statutes taxing interstate commerce must comply with three requirements: (1) they must be structured to prevent the possibility that interstate commerce will be taxed more than once on its full value; (2) they must not discriminate against interstate commerce in favor of intrastate commerce; and (3) they must impose a tax which is measured in some fair relation to the extent of the State's contact with the interstate commerce. *American Trucking Associations, Inc.* v. *Scheiner*, 107 S. Ct. at 2839, 2841; *Commonwealth Edison Co.* v. *Montana*, 453 U.S. 609, 626, 629 (1981); *Complete Auto Transit, Inc.* v. *Brady*, 430 U.S. at 279. Here Illinois has levied a tax on interstate communication which violates all three of these constitutional requirements.

At the outset, the State insists that it has not taxed interstate commerce at all, but rather has taxed only the "local" purchase of calls in Illinois. This is "mental gymnastics" of the kind disapproved by this Court in *Nippert* v. *City of Richmond*, 327 U.S. 416, 423 (1946). As both lower courts found, the language and practical effect of Illinois' statute makes unmistakable that it has taxed the *entire value* of interstate communications that, by definition, occur only partly within the State.

By laying its tax on the entire value of interstate communications, Illinois has violated the first key constitutional requirement for the tax—that it be "fairly apportioned" in order to avoid multiple taxation of the communications. If Illinois may tax 100 percent of the value of those interstate communications—even though part of the communications are necessarily attributable to activities in other States—there is no sound basis upon which to deny those other States the same right also to tax the same commerce at its full value. The inevitable result would be to permit the commerce to be burdened with multiple taxation.

Contrary to the lower court's view, nothing in Illinois' credit provision prevents this multiple taxation from occurring. At most, that provision permits an individual Illinois taxpayer—who has already paid Illinois' unapportioned tax—to seek a credit when that same taxpayer is taxed again on a given communication. The provision does nothing to prohibit other States from laying their own taxes on other persons who participated in the *same* communication; and it certainly offers no credit in such circumstances. Indeed, if Illinois' rule is adopted, repeated taxation of all forms of interstate communication would not only be authorized but encouraged, producing the precise economic dislocations the Commerce Clause was designed to prevent. To cure this constitutional violation, Illinois should be required to apportion its tax on interstate communications—just as other States are now doing—and to let retailers bill consumers for the particular tax each participating State chooses to levy on its proportionate share of each communication—as GTE has shown retailers have the capability to do.

Even if Illinois' credit provision were sufficient to legitimate its unapportioned tax on interstate communications, that provision cannot rectify Illinois' decision to lay the same five percent tax on interstate and intrastate communications alike. Although applying the same five percent rate appears facially neutral, in effect it is discriminatory because greater in-state services are necessarily provided to the intrastate than the interstate com-

munications. Charging the same rate for lesser services is the economic equivalent of charging a higher rate for the same services. In either case, unconstitutional discrimination against interstate commerce is the result.

Finally, Illinois' decision to charge a constant five percent rate on the full price of interstate communications—no matter what proportionate part of the communications occurs in Illinois or what amount of services Illinois has rendered to facilitate the communication—violates this Court's third important constitutional requirement: that Illinois measure its tax in some fair relation to the services it has provided in connection with the interstate commerce. Far from meeting this requirement, Illinois' statute in fact imposes a tax which is *inversely* related to the services the State has rendered. Thus, the *greater* the total distance traveled by the interstate communication—and thus the *lesser* Illinois' proportionate contribution to and contact with the communication—the *higher* will be Illinois' tax. This will necessarily be so because the constant five percent rate causes the Illinois tax to rise with the price of the communication, even as Illinois' proportionate contribution to the communication falls. In effect, therefore, as the price of a given communication rises (due to its increased interstate transmission), Illinois taxes for itself services provided by other States.

While the lower court excused this violation on the ground that the services provided by other States are "too speculative to override the substantial benefits extended by Illinois," this excuse should not be accepted. The components of interstate phone calls (origination, transmission, and receipt) and the services associated with those components are certaintly not speculative; they are documented and well known. Furthermore, inasmuch as Illinois taxes calls whether it is the originating *or* receiving State, it cannot be said that whatever services are rendered by other States to facilitate those calls do not justify taxation. If this is true, then the services

provided by Illinois must (at least in some cases) likewise be too speculative to justify taxation. Indeed, Illinois' reasoning is simply another invitation for multiple taxation: for if Illinois (as originating *or* receiving State) can tax the full value of a given communication on the ground that the State at the other end has rendered only speculative services, that other State can with equal right make the same claim and levy the same tax.

ARGUMENT

I. The Act Imposes A Tax On Interstate Telecommunications

Throughout this litigation—both in the Circuit Court, again in the Illinois Supreme Court, and most recently in its Motion to Affirm filed in this Court—the State's primary contention has been that no tax has been laid on interstate commerce at all. The State has consistently argued that only "local events" have been taxed by Illinois.[8] This Court long ago admonished the lower courts to be skeptical of such efforts to exempt state taxes from the dictates of the Commerce Clause. As the Court held in *Nippert* v. *City of Richmond*, 327 U.S. at 423:

> If the only thing necessary to sustain a state tax bearing upon interstate commerce were to discover some local incident which might be regarded as separate and distinct from "the transportation or inter-

[8] Thus, in its Motion to Affirm the State contended that the sole "taxable event" under the Act is "the origination or receipt in Illinois of a telephone call—singularly local events," and that the Act is limited to "the taxpayer's activity in Illinois." Motion to Affirm at 5, 15.

The court below made note of the State's repeated efforts to recast the statute as a purely local tax: "[T]he Director has applied various designations to the tax in issue. For example, the tax has been denominated as a 'purchase tax,' 'a use tax, *i.e.*, use of [a] privilege,' 'a tax on the privilege or act of using telecommunications within this State,' 'a consumption tax,' and a tax on the 'act, or * * * privilege of consuming messages.'" GA 8a-9a.

course which is" the commerce itself and then to lay the tax on that incident, all interstate commerce could be subjected to state taxation and without regard to the substantial economic effects of the tax upon the commerce. For the situation is difficult to think of in which some incident of an interstate transaction taking place within a state could not be segregated by an act of mental gymnastics and made the fulcrum of the tax. * * * [T]here is no known limit to the human mind's capacity to carve out from what is an entire or integral economic process particular phases or incidents, label them as "separate and distinct" or "local," and thus achieve its desired result.

Consistent with *Nippert*, both lower courts flatly rejected the "mental gymnastics" which would be necessary to make this tax a purely "local" one; instead, looking to the language of the statute and to its practical effects, those courts found that the Legislature clearly intended—and unquestionably achieved—a tax on interstate commerce. Examination of the statute leaves no doubt that the courts were correct. Section 4 of the Act provides that

> A tax is imposed upon the act or privilege of originating in this State or receiving in this State interstate telecommunications by a person in this State at the rate of 5% of the gross charge for such telecommunications purchased at retail from a retailer by such person. [GA at 29a.]

As the Act states, the five percent tax is levied on the "gross charge" for interstate telecommunications originated or received in Illinois. Section 2(a) in turn defines that "gross charge" as "the amount paid for the act or privilege of originating or receiving telecommunications in this State *and for all services and equipment provided in connection therewith* * * *." GA 25a (emphasis supplied). As both the trial court and the court below recognized, the "services and equipment provided in connection" with the telecommunication necessarily

include services and equipment being provided *outside* the State of Illinois. Thus, the trial court determined:

> Those words [of Section 4] unmistakably mean that *the taxable transaction is the interstate phone call.* * * * *
>
> [I]t is the phone call which is taxed and not the sale or purchase of that call.
>
> Five percent of the *gross charge* makes it clear that the call itself and not its billing in Illinois is what is really being taxed and *that event is an interstate activity.*
>
> In an attempt to tax some local aspect of an interstate phone call, the state asks the Court to focus on one-half of what goes on during that event, that is, the originating or receipt of a phone call to or from out of state, and then the state seeks to combine that half of a transaction with the billing of the same so as to make the entire transaction an Illinois transaction.
>
> The bill, of course, reflects the other out-of-state half of the transaction and in taxing five percent of the *entire* bill it's apparent that *the state is taxing activities which take place outside of Illinois.* [GA 20a-21a (emphasis supplied).]

As indicated above, the Illinois Supreme Court agreed with this analysis. Thus, when the State attempted to argue on appeal that what the Act taxes is a "purchase" in Illinois of a long distance telephone call, the Illinois Supreme Court expressly rejected such an interpretation:

> Thus, the fact that section 4 establishes the purchase price of an interstate telecommunication as the basis upon which the tax is calculated does *not* transform the taxable event into a retail purchase which, by definition, is local, apportioned, nondiscriminatory and fairly related to services provided by Illinois as required by *Complete Auto.* * * * A person simply cannot make or receive an interstate telecommunication without activating and partici-

> pating in a complex network of interstate transmissions culminating in interstate communication. We believe that such interstate communication *is* interstate commerce. The very process of interstate telecommunication is interstate commerce. [GA 9a (emphasis supplied).]

In so ruling, the court below recognized what this Court has held for more than a century—that a tax on the *entire cost* of an interstate telecommunication is necessarily a tax on interstate activity itself. *Telegraph Co.* v. *Texas*, 105 U.S. 460 (1881); *Fisher's Blend Station, Inc.* v. *Tax Commission*, 297 U.S. 650, 654 (1936) ("sending telegraph or telephone messages across state lines * * * is interstate commerce"). This construction of the Act by the lower court is clearly correct and should be affirmed by this Court.[9]

II. The Tax Is Completely Unapportioned And Necessarily Subjects Interstate Commerce To Multiple Taxation

Having determined that the Act lays a tax on "the entirety of each and every interstate telecommunication," it was inevitable that the lower court would also determine that the Act does not meet the "fair apportionment"

[9] Of course, the "practical effect" of the Illinois statute—not its language—ultimately governs its constitutionality, and that effect is for this Court finally to determine. *See, e.g.*, *American Trucking Associations, Inc.* v. *Scheiner*, 107 S. Ct. at 2841; *Maryland* v. *Louisiana*, 451 U.S. 725, 726 (1981); *Complete Auto Transit, Inc.* v. *Brady*, 430 U.S. at 279, 281. Nevertheless, in determining that practical effect—particularly in deciding whether the statute's effect is to tax the *whole* of interstate telecommunications rather than a purely local incident thereof—this Court should be guided by the lower courts' determination that the statute was intended by the Illinois Legislature to tax the *whole* of the interstate commerce at issue. The latter determination is a question of state law on which the Illinois Supreme Court's decision is dispositive. *Hortonville Joint School District No. 1* v. *Hortonville Education Association*, 426 U.S. 482, 488 (1976) ("We are, of course, bound to accept the interpretation of Wisconsin law by the highest Court of the State").

requirement of *Complete Auto*. GA 10a. Indeed, far from being a fairly apportioned tax, the lower court was forced to acknowledge that the tax at issue "is not an apportioned tax" at all. GA 10a.

This determination should have led the lower court to reject the tax. As this Court's cases have long made clear, if one State may permissibly tax more than its proportionate share of an interstate commercial activity, so too may all other States with a sufficient nexus with that activity. The inevitable result would be to subject the interstate activity to multiple taxation—taxation that intrastate activity would be spared.

Thus, as this Court stated in *Japan Line, Ltd.* v. *County of Los Angeles*, 441 U.S. 434 (1979):

> It is a commonplace of constitutional jurisprudence that multiple taxation may well be offensive to the Commerce Clause. In order to prevent multiple taxation of interstate commerce, this Court has required that taxes be apportioned among taxing jurisdictions, so that no instrumentality of commerce is subjected to more than one tax on its full value. *The corollary of the apportionment principle, of course, is that no jurisdiction may tax the instrumentality in full.* [*Id.* at 446-447 (emphasis supplied) (citations omitted).]

The Court has frequently reiterated this apportionment requirement,[10] and has applied it in circumstances much like the present case.

For example, the Court recognized in *Western Live Stock* v. *Bureau of Revenue*, *supra*, that:

> A tax on gross receipts from tolls for the use by interstate trains of tracks lying wholly within the

[10] *See, e.g.*, *Mobil Oil Corp.* v. *Commissioner of Taxes*, 445 U.S. 425, 444 (1980) ("Taxation by apportionment and taxation by allocation to a single situs are theoretically incommensurate"); *Exxon Corp.* v. *Department of Revenue of Wisconsin*, 447 U.S. 207, 230 (1980).

taxing state is valid, *New York, L.E. & W.R. Co.* v. *Pennsylvania*, 158 U.S. 431; *cf. Henderson Bridge Co.* v. *Kentucky*, 166 U.S. 150, although a like tax on gross receipts from the rental of railroad cars used in interstate commerce both within and without the taxing state is invalid. *Fargo* v. *Michigan, supra.* In the one case the tax reaches only that part of the commerce carried on within the taxing state; in the other *it extends to the commerce carried on without the state boundaries, and, if valid, could be similarly laid in every other state in which the business is conducted.* [*Id.* at 257 (emphasis supplied).]

Similarly, in *Central Greyhound Lines* v. *Mealey*, 334 U.S. 653 (1948), the Court struck down New York's unapportioned tax on the gross charge for a bus trip which originated and terminated in New York, but which also passed through New Jersey and Pennsylvania:

> If New Jersey and Pennsylvania could claim their right to make appropriately apportioned claims against that substantial part of the business of appellant to which they afford protection, we do not see how on principle and in precedent such a claim could be denied. This being so, to allow New York to impose a tax on the gross receipts for *the entire mileage*—on the 57.47% within New York as well as the 42.53% without—would subject interstate commerce to the unfair burden of being taxed as to portions of its revenue by States which give protection to those portions, as well as to a State which does not. [*Id.* at 662 (emphasis supplied).]

Likewise, in *Michigan-Wisconsin Pipe Line Co.* v. *Calvert*, 347 U.S. 154 (1954), the Court addressed an attempt by Texas to tax the "first taking" of the total volume of natural gas into an interstate pipeline for interstate transmission, a situation much like the "origination" of interstate telecommunications in the case at bar. The Court once again declared that no State may constitutionally arrogate to itself the power to tax the total value of an interstate transmission:

> [F]or if Texas may impose this "first taking" tax *measured by the total volume of gas so taken*, then Michigan and the other receipient states have at least *equal* right to tax the first taking or "*unloading*" from the pipeline of the same gas when it arrives for distribution. Oklahoma might then seek to tax the first taking of the gas as it crossed into that State. The net effect would be substantially to resurrect the customs barriers which the Commerce Clause was designed to eliminate. [347 U.S. at 170 (emphasis supplied).]

The court below ignored the teachings of all these cases and simply declared that "[a]n unapportioned tax * * * is not necessarily invalid," but is merely "constitutionally suspect because of the risk of multiple taxation." GA 10a, 11a. Even if a wholly unapportioned tax could be sustained on the ground that no "risk of multiple taxation" existed—a result that is without precedent in this Court's decisions [11]—that risk is clearly presented by the

[11] The court below could cite no case in which this Court has upheld a wholly unapportioned tax on interstate commerce. Ironically, the sole authority upon which the court below relied for the proposition that "An unapportioned tax, however, is not necessarily invalid" (GA 10a)—*Wisconsin Telephone Co.* v. *Wisconsin Department Of Revenue*, 125 Wis.2d 339, 371 N.W.2d 825 (1985)—was a Wisconsin appellate court decision that placed principal reliance on two cases, the reasoning of which has been rejected by this Court. The *Wisconsin Telephone* case relied upon an Alaska case—*Douglas* v. *Glacier State Telephone Co.*, 615 P.2d 580 (1980)—which, although decided three years after this Court's decision in *Complete Auto*, made its Commerce Clause analysis without so much as a citation to *Complete Auto*. *Douglas* rested its analysis, *inter alia*, on the assumption that a taxpayer had to show a "tangible likelihood" that multiple taxation would result, *id.* at 587; four years later, this Court rejected such a test in *Armco Inc.* v. *Hardesty*, 467 U.S. 638 (1984). The other case principally relied on by the *Wisconsin Telephone* court was *General Motors Corp.* v. *Washington*, 377 U.S. 436 (1964), which was expressly overturned last term in *Tyler Pipe Industries, Inc.* v. *Washington State Department Of Revenue*, 107 S.Ct. at 2816-17.

unapportioned tax in this case. Although the court below offered two reasons why it thought Illinois had successfully removed the risk of multiple taxation, neither reason is valid.

First, with respect to interstate calls *originated* in Illinois, the lower court concluded there was no risk of multiple taxation because it believed that "no other taxing entity could levy a tax on this taxable event." GA 11a. It is not certain what the court meant by this. If the court meant that no other State could tax the isolated act of originating a call in Illinois, that may be so; but it is plainly irrelevant, for that is not what Illinois has done. As the court below itself expressly and correctly determined, "the instant tax applies to *the entirety* of each and every interstate telecommunication"—not merely to origination—and for that very reason "it is not an apportioned tax." GA 10a (emphasis supplied). If, on the other hand, the court meant that no other State could tax any part of calls which originate in Illinois, it was clearly wrong.

It is certain that for every interstate call originating in Illinois, at least one other State (the receiving State) has a sufficient nexus with that call to impose a tax on its proportionate share of the call.[12] Indeed, in the case

[12] Whether or not other States are in fact now taxing calls that originate in Illinois is not constitutionally relevant. The risk of multiple taxation, not the fact, is sufficient to preclude a wholly unapportioned tax such as the present one. Otherwise, as the Court has specifically held, the constitutionality of each State's tax laws "would depend on the shifting complexities of the tax codes of 49 other States, and * * * the validity of the taxes imposed on each taxpayer would depend on the particular other States in which it operated." *Armco Inc.* v. *Hardesty*, 467 U.S. at 644. *See Tyler Pipe Industries, Inc.* v. *Washington State Department of Revenue*, 107 S.Ct. at 2820. Moreover, even if other States chose to "forego * * * entirely" their right to tax the value of interstate calls occurring within their borders, this would not authorize Illinois to tax the entirety of that value for itself. *Cf. American Trucking*

of a conference call occurring in several areas of the country at once, a call originated in Illinois would be taxable by a number of different States. And if any *one* of those States were permitted to tax the entire unapportioned value of the call—which is what Illinois seeks in this case—no principled basis would exist for denying that right to *every* other State involved with the call. It is this fact which presents the inevitable risk of multiple taxation; which condemned the nearly identical taxes described in *Central Greyhound*, *Western Livestock*, and *Michigan-Wisconsin Pipeline*; and which should have condemned the tax in this case. The court below was simply wrong to suppose that no other State could tax calls originated in Illinois and that this "fact" excused Illinois' failure to meet the "fair apportionment" requirement of *Complete Auto*.[13]

The court below was also wrong in its second asserted justification for this unapportioned tax, *i.e.*, that the Illinois credit provision effectively prevents any multiple taxation of interstate communications. According to the lower court, in the case of Illinois' "tax levied on the reception * * * of an interstate telecommunication," there is "a real risk of multiple taxation" because "at least two taxing jurisdictions [Wheat Ridge and Greeley, Colorado] levy a tax similar to the instant tax * * *." The court concluded that "[c]learly, this is multiple taxation * * * prohibited by the commerce clause, as inter-

Associations, Inc. v. *Scheiner*, 107 S. Ct. at 2840 n. 15; *Central Greyhound Lines, Inc.* v. *Mealey*, 334 U.S. at 663 ("even if neither Pennsylvania nor New Jersey sought to tax their proportionate share of the revenue from [the interstate commerce], such abstention would not justify the taxing by New York of the entire revenue").

[13] The Act itself demonstrates that States other than the State of origination can levy a tax on interstate telecommunication, for Illinois also levies its tax on calls that originate elsewhere and are received in Illinois, so long as the call is charged to an Illinois address. Ill. Rev. Stat. ch. 120 ¶ 2004; GA 29a.

preted by *Complete Auto* and its progeny * * *." GA 12a. Nevertheless, the court reasoned that the Illinois tax escaped this constitutional prohibition because "section 4 provides a credit against any tax due from a taxpayer who has paid two or more taxes on the same interstate telecommunication." This credit provision, the court held, "cures *any possible constitutional infirmity* resulting from the multiple taxation." GA 13a (emphasis supplied). As we will show, the credit provision does not—and could not—accomplish the necessary cure.

At the outset, the lower court significantly understated the number of interstate communications the credit provision would need to protect from multiple taxation in order to save Illinois' unapportioned tax. It is clear the court thought that, at most, only calls *received* in Illinois would need the protection of the credit provision.[14] But, as we have shown—and as the court's own opinion elsewhere makes clear—the Illinois tax is levied on the *entirety* of all interstate calls charged to an Illinois address, regardless whether the calls are originated or received in the State. Accordingly, other States participating in *all* such calls have a right to tax those calls.[15] As a result, even under the lower court's own standard, Illinois' unapportioned tax on such calls must be struck down unless the credit provision in fact prohibits multiple taxation on any of them. While it is difficult to

[14] Indeed, the language of the court's opinion suggests that it may have thought the credit provision was triggered only in the case of taxes on the event of *receipt* of calls in Illinois, as opposed to taxes on *calls* received in Illinois. See GA 12a. Whichever view the court took, its analysis was too restrictive.

[15] The lower court may have limited its credit analysis to calls *received* in Illinois because those calls were the only ones specifically shown to be the current subject of multiple taxation. If that was the rationale for the court's limitation, it was in error; as previously discussed, a statute which *permits* multiple taxation is constitutionally prohibited whether or not such multiple taxation has in fact already occurred. *See* n. 12, *supra*.

imagine how *any* credit provision could achieve that purpose, for several reasons it is patent that the one at bar does not.

The first and most significant failure in Illinois' credit provision is that by its very terms it does not protect *interstate commerce* from multiple taxation at all; instead, the statute is narrowly drawn to protect only *Illinois taxpayers*. At most, the Act affords a credit to an Illinois taxpayer only where that taxpayer has already paid Illinois' unapportioned tax on a given call, and is thereafter legitimately assessed an additional tax by another State or States on the same call. Ill. Rev. Stat. ch. 120, ¶¶ 2004 and 2002(h); GA 29a-30a, 27a. Thus, the credit provision has *no application whatever* where other States choose to tax their own taxpayers for calls they exchange with Illinois' taxpayers.

Accordingly, if such a narrow credit provision were held sufficient to validate this unapportioned tax, the necessary implication would be that the full, unapportioned value of interstate communications may be repeatedly taxed by successive States, so long as each State taxes a different participant involved in the communication. For example, in the case of a conference call involving a dozen participants in a dozen different States, under the lower court's decision each State would be invited to lay a tax on the full value of the call on the participant within its borders. Thus, far from *negating* the possibility of multiple taxation, the lower court's decision—if upheld—would *encourage* such taxation.

Obviously, the underlying assumption in the lower court's analysis of the credit provision is that multiple, unapportioned taxation of a single *interstate activity* is permissible, so long as no single *taxpayer* is taxed more than once. This assumption is clearly fallacious. This Court's Commerce Clause cases are concerned with whether *interstate commerce* has been permissibly taxed,

not with who ultimately pays the tax. *See, e.g., Evansville-Vanderburgh A.A. Dist.* v. *Delta Airlines, Inc.*, 405 U.S. 707, 714-715 (1972) ("Our inquiry is whether the use of airport facilities occasioned by enplanement is a permissible incident on which to levy * * * fees, regardless of whether the airline or its passengers bear the formal responsibility for their payment"); *Bacchus Imports, Ltd.* v. *Dias*, 468 U.S. 263, 268 n.8 (1984) ("Our cases make clear that discrimination between in-state and out-of-state goods is as offensive to the Commerce Clause as discrimination between in-state and out-of-state taxpayers"); *Japan Line, Ltd.* v. *County of Los Angeles*, 441 U.S. at 447 (apportionment required to ensure that "no *instrumentality of commerce* is subjected to more than one tax on its full value") (emphasis supplied).

The reason the Court has repeatedly indicated that it is the commerce which the Constitution protects from multiple taxation—not particular taxpayers—is that regardless of which taxpayers bear the ultimate economic cost of multiple taxation on such commerce,[16] the economic effect will be the same.[17] Here, for example, the inevitable effect of repeated taxation would be to raise the cost of interstate calls relative to intrastate calls and thereby unfairly burden interstate commerce.[18] As the

[16] As noted, Illinois requires long-distance carriers to remit any tax due from the taxpayer, whether or not the taxpayer actually pays the tax. No credit is provided such a carrier even if it pays an additional tax to another State.

[17] This Court has repeatedly recognized that the overall "economic effect" of a State's tax is the appropriate focus. *See, e.g., Westinghouse Electric Corp.* v. *Tully*, 466 U.S. 388, 404 (1984).

[18] As Professor Samuelson has noted, the imposition of a tax on any commodity "will raise the price to consumers and lower the price received by producers, the difference going to government. At the higher price a smaller quantity will be bought by consumers." P. Samuelson, *Economics*, p. 366 (11th ed. 1980). Accordingly, once any new tax has been levied on interstate calls—a tax to which intrastate calls are not subjected—it will inevitably

Court reiterated in *Armco Inc.* v. *Hardesty*, "'[i]f another State has taxed *the same interstate transaction*, the burdensome consequences to interstate trade are undeniable.'" 467 U.S. at 645 n.8 (emphasis supplied) (quoting *Freeman* v. *Hewit*, 329 U.S. 249, 256 (1946)).[19]

Moreover, it would be difficult to overstate the total "burdensome consequences" and economic dislocations that could result if the Court affirms the unapportioned tax in this case. Much more is involved here than a single State's tax on interstate telephone calls.[20] If Illinois is permitted to lay an unapportioned tax on interstate calls so long as it protects *its own* taxpayers from repeated taxes, so too can the other 49 states. Furthermore, the authorized unapportioned taxes in the 50 states would not be limited to telephone calls. As the statute in this case demonstrates, approval of the present unapportioned tax invites similar taxes on the limitless variety of communications that are now, and will be, criss-crossing this country, including:

> messages or information transmitted through use of local, toll and wide area telephone service; private line services; channel services; telegraph services; tele-typewriter, computer exchange services; cellular

follow that fewer and/or shorter interstate calls will be made, that the quality of interstate service will be jeopardized as carriers seek ways to compensate for the reduction in revenues, and that intrastate communications will have been effectively subsidized.

[19] This Court long ago recognized that "where the burden of a tax falls on a thing which is the subject of taxation the tax is to be considered as laid on the thing rather than on him who is charged with the duty of paying it into the treasury." *Telegraph Co.* v. *Texas*, 105 U.S. 460, 465 (1881). The Circuit Court was clearly correct, therefore, when it held that "[t]he relevant inquiry is as to just *what* is being taxed and not *who* is being taxed. * * *." GA 21a (emphasis supplied).

[20] And, as previously stated (see n.2), the telephone tax in Illinois alone, limited to the period since August 1, 1985, had already generated 142 million dollars as of July 1987.

mobile telecommunications service; specialized mobile radio; stationary two-way radio; paging service; or any other form of mobile and portable one-way or two-way communications; or any other transmission of messages or information by electronic or similar means, between or among points by wire, cable, fiber-optics, laser, microwave, radio, satellite or similar facilities. [Ill. Rev. Stat. ch. 120, ¶ 2002; GA 26a.]

If every State were permitted to charge a tax on the full value of all such forms of interstate communication to every in-state taxpayer who participated in the communication, the possibilities for cumulative multiple taxation would be staggering; taxes in excess of the underlying charge for the communication services would not be far-fetched at all. As this Court stated in *Armco*, the "burdensome consequences"—particularly to this burgeoning area of interstate commerce—would be "undeniable." 467 U.S. at 645 n.8.

Moreover, if this Court approved a State's unapportioned tax on the basis of a credit provision like the one in this Act—which effectively offers to transfer the *entire* tax on a given interstate communication to any other State laying an equal or greater tax on the same taxpayer—the result would be to award the whole of the tax on interstate commerce to a single State, even though several States may have contributed to the commerce. This directly undermines the "fair apportionment" standard *Complete Auto* and its progeny were designed to foster.

Finally, even if the Court were otherwise inclined to uphold an unapportioned tax where a credit provision guaranteed that no single *taxpayer* would be subjected to multiple taxation, Illinois' credit provision presents no such guarantee. The tax-and-credit scheme provided for here is fundamentally different from the normal situation where a taxpayer obtains a credit against another tax, such as in the case of use and sales taxes. In those situations, the taxpayer himself has paid the tax and knows that the first tax has been paid when he is called upon to pay the second tax. Moreover, in those situations, the taxpayer is not required to pay the second tax in full and then seek to obtain a "credit"; rather, the second tax is simply reduced by the amount of the first at the time the second tax is paid. *Compare American Trucking Associations, Inc.* v. *Scheiner*, 107 S. Ct. at 2834-35.

In the case at bar, however, there is not even an absolute requirement that the taxpayer be informed of the amount of tax imposed on him by this Act,[21] much less any assurance that he will know of a tax imposed by *another* State on the same call. And when the taxpayer pays the tax under this Act, he pays it *not* to the party from whom he must later attempt to obtain the "credit" (the State), but rather to the long distance carrier. When all of this is considered in the context of the fact that the Act contains no procedures whatever for actually obtaining the "credit," Illinois' taxing scheme should be deemed so ineffective and burdensome as not to meet the demands of the Commerce Clause. *Cf. Nippert* v. *City of Richmond*, 327 U.S. at 430 n.21. This should particularly be so where, as here, the State has sought to justify an otherwise unapportioned, unconstitutional tax on the ground that its credit provision assures that no multiple tax can possibly result. Illinois' credit scheme does not offer any such assurance.

For all the foregoing reasons, the existence of the "credit" referred to in Section 4 of the Act cannot remove the risk—indeed the likelihood [22]—of multiple taxa-

[21] The Act provides only that it be disclosed "[w]henever possible." Ill. Rev. Stat. ch. 120, ¶ 2005; GA 30a.

[22] The subject of interstate telecommunications taxation has become a principal focus of taxing authorities throughout the country, and it is clear that taxes on interstate telecommunications—of all sorts—will proliferate as State and local taxing

tion that results from Illinois' imposition of an unapportioned tax on interstate commerce. It bears emphasis that the dispute does not center on whether an apportionment by Illinois of that portion of the transaction fairly allocable to Illinois has been fairly calculated. We understand that "extreme nicety is not required" in making this allocation,[23] but here Illinois has made *no attempt*

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authorities intensify their search for new sources of revenue. *See, e.g., The Taxation Of Telecommunications: In Ohio,* NATA Conference on Revenue Estimating, November 1-4, 1987; *Unitary Method, Florida Sales Tax, Telecommunications Taxes Focus of FTC Meeting,* 36 Tax Notes, No. 3, p. 249, July 20, 1987; *The Challenge Of Telecommunications: State Regulatory And Tax Policies For A New Industry,* edited by Barbara Dyer, December 15, 1986; *Final Report Of The Connecticut Telecommunications Task Force,* Finance, Revenue and Bonding Committee, Connecticut General Assembly, January 1986; *Florida Telecommunications Task Force Final Report To Governor Bob Graham And The Florida Legislature,* February 1, 1985.

[23] *Smith* v. *Illinois Bell Telephone Co.*, 282 U.S. 133 (1930). In *Smith*, the District Court had found that interstate long distance telecommunication then made up a miniscule percentage of the total use of the local network facilities: one-half of one percent of all originated calls. *Id.* at 147. It therefore had decided that "as a matter of convenience, in view of the practical difficulty of dividing the property between the interstate and intrastate service," such apportionment was not required. *Id.* at 150. This Court unanimously reversed, concluding that whatever the practical difficulties of separating costs, such separations were required to avoid discrimination: "While the difficulty in making an exact apportionment of the property is apparent, and extreme nicety is not required, only reasonable measures being essential, *it is quite another matter to ignore altogether the actual uses to which the property is put.*" *Id.* at 150-151 (emphasis supplied) (citations omitted).

The *Smith* decision still guides the telecommunications industry today. After *Smith*, the States, the FCC, and telephone companies developed standard methodologies for apportioning the costs of property between interstate and intrastate, generally based on relative usage of the specific facilities. These apportionment principles necessarily make use of reasonable assumptions and estimates

whatsoever to fairly apportion the amount of the charge for the communications attributable to services provided by Illinois.

Illinois' action should be contrasted with the approach other States have taken. For instance, Florida has adopted an apportionment formula in its tax on interstate privateline communications "to ensure that no more than 100 percent of the interstate interoffice channel mileage charge can be taxed by this state and another state." Fla. Stat. Ann. § 212.05(1)(e)2c. Similarly, New Mexico provides that its gross receipts tax on interstate telecommunications shall apply to sixty-five percent of receipts from long-distance interstate and foreign calls that either originate or terminate in New Mexico and are billed to a New Mexico account or number. N.M. Stat. Ann. § 7-9-56(C). Likewise, Virginia applies its gross receipts tax on interstate telecommunications on the basis of a comparison of the carrier's circuit capacity in Virginia with its capacity systemwide. Va. Code §§ 58.1-2623 and 58.1-2624. *Cf. South Cent. Bell Telephone Co.* v. *Celauro*, 735 S.W.2d 228 (Tenn. 1987) ("end-user charge" on long-distance calls permitted only because the charge was fairly apportioned to services rendered in Tennessee).

These other States' efforts to avoid multiple taxation of interstate commerce may or may not pass constitutional muster. But at least these States recognize that *some* apportionment effort must be made and that no one State can arrogate to itself the right to tax the entire value of an interstate communication. Illinois, in contrast, wants it all. And inasmuch as Illinois' credit provision fails to remove the threat of multiple taxation and otherwise completely subverts the requirement of "fair

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which have been adjusted over time as interstate long-distance service has developed from an expensive luxury to a commonplace of modern life. But the core necessity of apportionment of costs has always been observed.

apportionment,"[24] the State's tax cannot be squared with the Commerce Clause. It should therefore be disapproved.

III. The Tax Discriminates Against Interstate Commerce

The lack of apportionment of the Illinois tax "is a form of discrimination against interstate commerce." *Armco Inc.* v. *Hardesty*, 467 U.S. at 644. This is because Illinois' tax subjects interstate calls to multiple taxation that local calls need not bear. Thus, a conference call among twelve Illinois cities will be taxed on its full value only once, at a rate of five percent. As explained above, however, if that conference call were among twelve cities in twelve different States, Illinois' approach invites each State to tax the call on its full value; this could easily produce a cumulative tax in excess of the cost of the call itself.

But that is not the only form of discrimination effected by the challenged tax. Even assuming that a credit provision such as Illinois' could avoid the risk of multiple taxation, that provision cannot absolve the statute from the other kind of discrimination it practices—charging interstate communications at a higher effective rate for services rendered than it charges intrastate communications.

The court below assumed that the Illinois tax did not discriminate against interstate commerce simply because

[24] Significantly, as GTE's uncontradicted evidence demonstrated in the trial court, carriers now have the capability to bill each telephone customer for whatever tax each participating State chooses to levy on its proportionate share of each call charged to the customer's account. "For example, GTE Sprint can bill an Illinois customer for an interstate telecommunication originating in Illinois and terminating in New York, and could include, in that charge, a tax assessed by Illinois, the originating state, and New York, the terminating state." GTE A 9a. In such circumstances, there can be no justification for Illinois' decision to tax the whole of interstate communications, rather than only its fair share.

Illinois taxed interstate and intrastate telecommunications at the same flat rate. GA 11a. As this Court emphasized in a recent opinion, however—an opinion that was not available to the court below when it issued its judgment—"the Commerce Clause has a deeper meaning that may be implicated even though state provisions * * * do not allocate tax burdens between insiders and outsiders in a manner that is *facially* discriminatory." *American Trucking Associations, Inc.* v. *Scheiner*, 107 S. Ct. at 2839 (emphasis supplied). In practice, Illinois' application of the same rate to all telephone calls in fact *ensures* discrimination, since Illinois necessarily provides greater services with respect to intrastate than interstate calls. The net result is that interstate calls are subject to greater taxation for the same services.

A variety of examples illustrates the inherent discrimination. Take two calls from Chicago, one to Joliet, Illinois, and the other to Gary, Indiana. Assume both calls cost two dollars. Each call is taxed ten cents by Illinois. Illinois provides origination, complete transmission, and receipt services for the intrastate call for that ten cents. The interstate call is subject to the same ten-cent tax but receives only origination and partial transmission services from the taxing State for its dime. It therefore pays more for those same services than the intrastate call.

The discrimination is inherent in the statute, since the Act imposes the same tax on interstate calls even though the State necessarily provides fewer services for such calls. This discrimination is more dramatically illustrated by considering a call from Chicago to a town on the western border of Illinois, costing, say, two dollars, and a call from Chicago continuing on from that town on the western border to Los Angeles, costing, say, five dollars. Both calls originate at the same point in Illinois and both are carried the same distance through Illinois. But the intrastate call is taxed ten cents for this service and the interstate call is taxed 25 cents. Because Illinois

imposes a higher charge on interstate calls for the same services (a result attributable to its taxing of activities beyond its borders), the charge necessarily discriminates in favor of purely local activity.

This Court confronted a similar problem in *Scheiner*. There Pennsylvania imposed the same axle tax on all vehicles, whether registered in Pennsylvania or outside the State. The lower court, like the court below here, sustained the tax as nondiscriminatory.[25] This Court reversed, finding that the facially neutral tax discriminated against the vehicles in interstate commerce: "In practical effect, since they impose a cost per mile on appellants' trucks that is five times as heavy as the cost per mile borne by local trucks, the taxes are plainly discriminatory." 107 S. Ct. at 2841.[26] So too here: the imposition by Illinois of the same flat tax on intrastate and interstate telecommunications results in a higher proportional cost being imposed on the interstate telecommunications. Such a result is "plainly discriminatory."[27]

[25] *Compare* GA 11a *with* 107 S.Ct. at 2838.

[26] Justice Stevens, who wrote the opinion for the Court in *Scheiner*, anticipated the reasoning adopted in that case when he noted earlier in *Mobil Oil Corp.* v. *Commissioner of Taxes*, *supra*:

> [I]f, in a particular case, use of [a particular taxing formula] has the effect of taxing income earned by an interstate entity outside the State, it could alternatively be said to have the effect of taxing the income earned by that entity inside the State at a rate higher than that used for a comparable, wholly intrastate business, a discrimination that violates the Commerce Clause. [445 U.S. at 452 (Stevens, J., dissenting).]

The same discrimination is presented here. Because Illinois in effect taxes interstate communications for out-of-state services, its rate of tax for its own in-state services is higher for those interstate communications than for wholly intrastate communications.

[27] Moreover, the less contact Illinois has with a particular interstate call, the more discriminatory its treatment of that call will become. Given that longer interstate calls carry a higher retail charge, the smaller a call's proportional contact with Illinois, the greater will be Illinois' tax. Conversely, in the case of the generally less expensive intrastate calls, where Illinois' contact is exclusive and its services at their apex, the tax will necessarily be less than for interstate calls, due to the constant five percent rate.

Thus, the Illinois tax discriminates against interstate commerce in two ways: first, by subjecting interstate calls to multiple taxation, it burdens those calls with costs that will not be borne by intrastate calls; second, even if no other State imposed a tax on the interstate calls—and hence no multiple taxation ever occurred—Illinois' flat tax on all calls effectively imposes a heavier burden on interstate calls for the same state services. Such discrimination is prohibited by the Commerce Clause.

IV. The Tax Is Not Fairly Related To Services Provided By Illinois

The fourth prong of the *Complete Auto* test requires that the tax on interstate commerce be "fairly related to the services provided by the State." 430 U.S. at 279. The "fair relation" element of the test demands that

> the measure of the tax must be reasonably related to the extent of the contact [with the taxing State], since it is the activities or presence of the taxpayer in the State that may properly be made to bear a "just share of state tax burden." [*Commonwealth Edison Co.* v. *Montana*, 453 U.S. at 626 (quoting *Western Live Stock* v. *Bureau of Revenue*, 303 U.S. at 254).]

Here the measure of the tax is clearly not "reasonably related" to the extent of contact with the taxing State. In fact, the measure is *inversely* related to the extent of contact; *i.e.*, as the contact of the interstate commerce with Illinois diminishes, the tax on that commerce *increases*.[28]

[28] The uncontradicted evidence submitted in the trial court established that

> The basic charge for an interstate toll call varies according to the distance between the place the call originates and the

This perverse result is a necessary consequence of the flat five percent tax and the State's decision to allocate to itself the entire value of interstate telecommunications. This Court observed this precise phenomenon forty years ago in setting aside New York's unapportioned gross receipts tax on interstate transportation in *Central Greyhound Lines* v. *Mealey, supra*:

> By its very nature, an unapportioned gross receipts tax makes interstate transportation bear more than "a fair share of the cost of the local government whose protection it enjoys." [334 U.S. at 663 (quoting *Freeman* v. *Hewit*, 329 U.S. at 253).]

A simple example will highlight the problem. The tax on a one-dollar call from Chicago to an Iowa town just over the border is five cents. The tax on a five-dollar call from Chicago to Los Angeles—involving proportionally much less contact with Illinois—is 25 cents. As the interstate aspects of the commerce grow, Illinois demands a greater tax based on the proportionally diminishing contact with Illinois. Since the measure of the tax is based on the entire value of the interstate telecommunication—including value attributed to activities outside Illinois—the greater the significance of those out-of-state activities, the higher the tax for the in-state activities. Accordingly, the Illinois tax, like the taxes at issue in *Scheiner*,

> does not vary with miles traveled or with some other proxy for value obtained from the State. "[W]hen the measure of a tax bears no relationship to the taxpayers' presence or activities in a State, a court may properly conclude under the fourth prong of the *Complete Auto Transit* test that the State is imposing an undue burden on interstate commerce." [*Scheiner*, 107 S. Ct. at 2844 (quoting *Commonwealth Edison Co.* v. *Montana*, 453 U.S. at 629).]

place it terminates, increasing in price as the distance between these points increases. The charge for an interstate private line call varies solely according to the length of the line utilized in the transmission. [GTE A 9a.]

The fourth prong of *Complete Auto* simply recognizes that a State may not tax activity outside its borders to which it has no legitimate claim, but must measure its tax in some form relative to the services it has provided.

To the extent that the court below gave any consideration to the fair relation requirement, it did so with reasoning that was internally inconsistent and a clear invitation to multiple taxation. It argued first that the services provided by Illinois "facilitate perhaps the most critical step in the taxable event—interstate origination." It next acknowledged that "[i]t is true that the State is taxing the 'gross charge' of the entire interstate telecommunication even though the benefits it affords are limited to that portion of the communication occurring within the State." The court then concluded that "the benefits afforded by other States in facilitating the same interstate telecommunication are too speculative to override the substantial benefits provided by Illinois." GA 13a.[29] It is not clear whether the court meant that other States' services are "too speculative" only when Illinois is the originating State, or also when it is the receiving

[29] The court below relied on *Western Live Stock* v. *Bureau of Revenue, supra*, for its "too speculative" language. *Western Live Stock* involved a tax on the amounts received from the sale of advertising space in a New Mexico magazine with an interstate circulation. The Court noted that the tax was not on the purchase (subscription) price of the magazine but rather on "the preparation, printing and publication of the advertising matter, and the receipt of the sums paid for it"—all of which "occur[red] in New Mexico and not elsewhere." 303 U.S. at 260. The Court thought that the extent to which those advertising rates reflected the interstate circulation was "too remote and too attenuated" to call for apportionment. *Id.* at 259.

In the case at bar the involvement of other States is neither remote nor speculative; it is palpable and admitted: "A person simply cannot make or receive an interstate telecommunication without activating and participating in a complex network of interstate transmissions culminating in interstate communication." GA 9a.

State. Whichever the Court meant, its conclusion is factually incorrect[30] and analytically unsound.

Illinois, of course, taxes the full value of interstate transmissions charged to an Illinois address whether it is the originating or receiving State. If the court meant that only a *receiving* State's services are "too speculative" to justify taxation, then Illinois—which taxes the entire values of calls received and charged in Illinois—cannot justify its own tax on such calls. On the other hand, if the court intended to declare that other States' services are "too speculative" whether Illinois were the originating *or* receiving State, the court has either implicitly condemned *all* of Illinois' taxes in this case or, alternatively, the court's reasoning (if accepted) would constitute a blanket endorsement of multiple taxation. Manifestly, if one State may simply declare that all out-of-state services associated with any given interstate call are "too speculative" to warrant consideration, so too may the other States connected with the same communication; and, accordingly, all such States may tax the entire value of the communication. This is plainly unacceptable.

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[30] There is nothing "speculative" about the services associated with interstate calls. A typical interstate call has three distinct segments: local originating access in State A, long-distance transmission from State A to State B (perhaps crossing several intermediate States), and local terminating access in State B. Significantly, each of these segments uses separate facilities and involves separate charges, even though the charges are usually bundled together when billed. The local telephone company in State A provides originating access service for the call and bills the long-distance carrier for that service at its tariff rates; the local telephone company in State B similarly provides the terminating access at its own different rates. The long-distance carrier then charges the customer the sum of the originating and terminating access rates plus its own rate for the interstate transmission segment. *See generally NARUC* v. *FCC*, 737 F.2d 1095, 1103-04 (D.C. Cir. 1984), *cert. denied*, 469 U.S. 1127 (1985). GTE Sprint introduced uncontradicted evidence to this same effect in the trial court. GTE A 7a-9a.

In any event, even if the services provided by one State (for example, the originating State) were more substantial than those provided by the receiving State, that fact would not allow Illinois to tax the *full* value of calls originating within its borders. The question is not whether the out-of-state benefits "override" the benefits provided by Illinois; the question, rather, is whether Illinois has devised a tax that fairly measures the benefits that *it* provides. As shown, Illinois has not. Indeed, it has devised no measure at all. The State's complete failure to measure its tax in some fair relationship to the services its provides renders the tax unconstitutional.

CONCLUSION

For the foregoing reasons, the judgment below should be reversed.

Respectfully submitted,

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Nos. 87-826, 87-1101

In The

Supreme Court of the United States

October Term, 1987

JEROME F. GOLDBERG, ROBERT McTIGUE
and GTE SPRINT COMMUNICATIONS CORPORATION,
Appellants,

v.

ROGER D. SWEET, Director of the Illinois
Department of Revenue, and JEROME COSENTINO,
Treasurer of the State of Illinois,
Appellees.

On Appeal from the
Supreme Court of Illinois

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QUESTION PRESENTED

The Illinois Telecommunications Excise Tax Act imposes a tax on "the act or privilege of originating or receiving" long distance telephone calls in Illinois. This tax places a five percent assessment on the entire gross charge for all long distance calls which either begin or end in Illinois and which are charged to an Illinois service address, but regardless of where such charges are billed or paid.

The Illinois statute acknowledges that other states may likewise seek to tax the calls taxed by Illinois. Indeed, several other states and municipalities have already passed taxes on long distance calls originating or terminating and billed or paid for within their boundaries. The Illinois tax provides that any taxpayer who thus pays tax both to Illinois and another state on the same long distance calling activity may obtain an Illinois tax credit. The credit is not measured by the amount of the Illinois tax, however, but by the amount of tax the taxpayer has paid to the state other than Illinois on the same calling activity. Obtaining this credit is contingent upon the taxpayer proving that the other state's tax: (a) has been imposed on the same event taxed by Illinois; (b) is "properly due;" and (c) has already been paid. The statute provides no criteria for determining whether another state's tax covers the same activity covered by the Illinois tax, or for determining when a tax in another state is "properly due."

The Illinois tax also places a five percent assessment on the gross charge for calls which occur entirely within the State of Illinois.

The question presented on this appeal is whether the Illinois tax, as applied to interstate long distance telephone calls as described above, violates the Commerce Clause of the Constitution of the United States.

LIST OF PARTIES AND CORPORATE AFFILIATIONS

A list of the parties to this proceeding is included in the Jurisdictional Statement previously filed by GTE Sprint Communications Corporation ("Sprint Jurisdictional Statement") at ii. A description of GTE Sprint's corporate affiliations, provided pursuant to United States Supreme Court Rule 28.1, was also included in the Sprint Jurisdictional Statement at 1, fn. 1.

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Nos. 87-826, 87-1101

In The

Supreme Court of the United States

October Term, 1987

JEROME F. GOLDBERG, ROBERT McTIGUE and GTE SPRINT COMMUNICATIONS CORPORATION,

Appellants,

v.

ROGER D. SWEET, Director of the Illinois Department of Revenue, and JEROME COSENTINO, Treasurer of the State of Illinois,

Appellees.

On Appeal from the Supreme Court of Illinois

BRIEF OF APPELLANT GTE SPRINT COMMUNICATIONS CORPORATION

OPINIONS BELOW

The opinion of the Illinois Supreme Court is reported at 117 Ill. 2d 493, 512 N.E.2d 1262 and is reprinted in the Appendix to the Jurisdictional Statement already filed in this Court by Appellants, Jerome F. Goldberg and Robert McTigue, in a related appeal now consolidated with GTE Sprint's appeal. *(Jerome F. Goldberg and Robert McTigue v. Roger D. Sweet, et al.*, No. 87-826 (docketed in the United States Supreme Court Nov. 20, 1987)). Goldberg J.S. App. C at 4a-16a.

The findings and opinion of the Circuit Court of Cook County, Illinois, dated October 22, 1986, are not reported.

A copy of the trial court's findings of fact and conclusions of law is included in Goldberg J.S. App. E at 18a-24a.

JURISDICTION

Appellants Jerome F. Goldberg and Robert McTigue (collectively "Goldberg") sued the Illinois Department of Revenue ("State of Illinois") in the Circuit Court of Cook County, Illinois, challenging the validity of the Illinois Telecommunications Excise Tax Act ("Tax Act") under the Illinois and United States Constitutions. GTE Sprint was named as a nominal defendant and filed a cross-claim against the State of Illinois, also challenging the constitutionality of the Tax Act.[1] The trial court granted motions filed by Goldberg and GTE Sprint for summary judgment, and held the Tax Act unconstitutional, on Commerce Clause grounds.

The State of Illinois appealed directly to the Illinois Supreme Court, which ultimately held the Tax Act constitutional despite the Commerce Clause challenge. The Illinois Supreme Court's judgment was entered on June 24, 1987, and an opinion supporting the judgment was filed on July 27, 1987. On July 15, 1987, GTE Sprint filed a timely petition for rehearing with the Illinois Supreme Court, which petition was denied on October 5, 1987. Sprint J.S. App. B at 6a.

On December 8, 1987, GTE Sprint filed with the Illinois Supreme Court its Notice of Appeal from the June 24 judgment, and on December 31 docketed that appeal here. Sprint J.S. App. A at 1a. This Court noted probable jurisdiction of GTE Sprint's appeal on February 22, 1988. Joint Appendix at 13a ("J.A."). The jurisdiction of this Court rests on 28 U.S.C. § 1257(2) (1982).

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[1] Illinois law affords parties the option of challenging taxes either through administrative or state court proceedings. Illinois State Officers and Employees Money Disposition Act, Ill. Rev. Stat. ch. 127, § 172 (1985). *Shell Oil Co. v. Department of Revenue*, 95 Ill. 2d 541, 449 N.E.2d 65, 66 (1983). Further, GTE Sprint has standing to challenge the Illinois tax under the Commerce Clause. *Bacchus Imports, Ltd. v. Dias*, 468 U.S. 263, 267 (1984).

CONSTITUTIONAL AND STATUTORY PROVISIONS

Commerce Clause, United States Constitution: "The Congress shall have Power . . . to regulate Commerce with foreign Nations, and among the several States . . . ." Art. I, § 8, cl. 3.

The full text of the Illinois Telecommunications Excise Tax Act, Ill. Rev. Stat. ch. 120, §§ 2001-2021 (1985) is set forth in Goldberg J.S. App. F at 25a-47a.

The relevant texts of several state taxing statutes and municipal ordinances, not directly at issue but referred to in the Sprint Jurisdictional Statement and herein, are included in the Sprint J.S. Appendices, Appendix D through H at 11a-22a and in the Appendices to this brief as Appendix B through E. A summary of selected statutes is included in Appendix A hereto.

STATEMENT OF THE CASE

A. GTE Sprint's Interstate Business and Operations[2]

GTE Sprint Communications Corporation is a retailer of intrastate and interstate telecommunications services. Sprint J.S. App. C at 7a; R. C 756. A large portion of GTE Sprint's business consists of providing paying customers interstate voice transmission services, by telephone, in all fifty states of the United States and in several foreign countries. Sprint J.S. App. C at 7a; R. C 756. In order to provide these services, GTE Sprint has established, over the years and at great expense, its own interstate transmission network comprised of microwave radio, fiber optic, satellite and cable facilities, spread over numerous states. Sprint J.S. App. C at 7a-8a; R. C 756.

In transmitting voice messages on an interstate basis, GTE

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[2] These facts were included in GTE Sprint's verified cross-claim and in an affidavit supporting GTE Sprint's cross-motion for summary judgment. *See* Sprint J.S. App. C at 7a-10a; R. C 116-127, 795-799. These facts have never been challenged by the State of Illinois.

Sprint utilizes its own transmission facilities where possible. However, GTE Sprint must also purchase the services of other telecommunications carriers to complete its transmissions in certain areas its network does not reach. Sprint J.S. App. C at 8a; R. C 756-757.

The total costs GTE Sprint incurs in sending its interstate transmissions stem from several sources -- from the costs of building and maintaining its interstate lines, the costs of sending transmissions over its interstate lines, the cost of purchasing the use of other carriers' lines in states where Sprint has not built lines, and the cost of access charges which must be paid to other carriers to pick up and drop off calls at the local level. Sprint J.S. App. C at 8a-9a; R. C 757. These are costs which GTE Sprint incurs in sending each interstate transmission and which emanate from activities occurring in each of the states involved in the path of the interstate transmission. Sprint J.S. App. C at 8a-9a; R. C 757.

These costs of interstate transmission are recovered by GTE Sprint from its customers in the tariffed prices the customers pay for telecommunications services. The customer's charge for an interstate toll call varies according to duration of the call and the distance between the place the call originates and the place it terminates; the call increases in price both as the duration of the call and the distance between these points increases. The transmission costs to GTE Sprint on long distance calls also increase the farther it must transmit each such call. Sprint J.S. App. C at 9a; R. C 757-758.

GTE Sprint is capable, administratively, of billing more than one state's tax on a single interstate communication. For example, GTE Sprint, in charging for an interstate transmission originating in Illinois and terminating in New York, could include in the charge for that call not only a tax assessed by Illinois, the originating state, but also a tax assessed by New York, the terminating state, as well as any tax assessed by any one state on the call's transmission path. Sprint J.S. App. C at 9a; R. C 758.

GTE Sprint's intrastate telecommunications services are provided pursuant to tariffs authorized by the Illinois Commerce Commission, while its interstate telecommunications services are common carrier services subject to Federal Communications Commission regulation, under 47 U.S.C. §§ 153 (e) and 201 *et seq*. Sprint J.S. App. C at 9a; R. C 758.

B. The Illinois Telecommunications Excise Tax Act

Section 4 of the Illinois Telecommunications Excise Tax Act provides:

> [A] tax is imposed upon the *act or privilege of originating in this State or receiving in this State interstate telecommunications* by a person in this State *at the rate of 5% of the gross charge* for such telecommunications purchased at retail from a retailer by such person.

Goldberg J.S. App. F at 29a; Ill. Rev. Stat. ch. 120, § 2004 (1985) (emphasis added). "Gross charge" is defined as "the amount paid for the act or privilege of originating or receiving telecommunications in this State . . . ." Goldberg J.S. App. F at 25a; Ill. Rev. Stat. ch. 120, § 2002(a) (1985). "Amount paid" is defined under the Act as "the amount charged to the taxpayer's service address in this State *regardless of where such amount is billed or paid.*" Goldberg J.S. App. F at 26a; Ill. Rev. Stat. ch. 120, § 2002(b) (1985) (emphasis added).

Section 4 of the Act contemplates that states other than Illinois will impose taxes on the same interstate calling activity taxed by Illinois and provides the following credit provision for those situations:

> To prevent actual multi-state taxation of the act or privilege that is subject to taxation under this paragraph, any taxpayer, *upon proof that that taxpayer has paid a tax in another state on such event, shall be allowed a credit* against the tax imposed in this Section 4 *to the extent of the amount of such tax properly due and paid in such other state.*

Goldberg J.S. App. F at 29a-30a; Ill. Rev. Stat. ch. 120, § 2004 (1985) (emphasis added).

C. Other Existing Taxes on Interstate Telecommunication Activity

During the past few years, numerous states and municipalities have enacted taxes on interstate telecommunications activity, which taxes are similar to the Illinois tax. A list and summary of some of these statutes is included in Appendix A hereto.

D. The Proceedings Below

Goldberg originally filed this lawsuit against the Illinois Department of Revenue, challenging the constitutionality of the Illinois Telecommunications Excise Tax Act under the United States and Illinois Constitutions. R. C 2. GTE Sprint and other long distance message carriers were named as nominal defendants, being retailers responsible for collecting the tax. GTE Sprint filed a cross-claim against the Illinois Department of Revenue and State Treasurer ("State of Illinois"), challenging the validity of the tax under (*inter alia*) the Commerce Clause of the United States Constitution. R. C 112-127. GTE Sprint simultaneously moved, under Illinois statute, to have an order of injunction entered requiring that the amounts it or its customers paid under the Tax Act be placed into a "protest fund" pending disposition of its tax challenge, to preserve the payments for refund if the Tax Act were ultimately declared unconstitutional. *See* Illinois State Officers and Employees Money Disposition Act, Ill. Rev. Stat. ch. 127, § 172 (1985); R. C 118-123. The trial court granted GTE Sprint's motion. R. C 134. Thereafter, a number of other carriers, including AT&T, MCI and others, filed similar cross-claims and requests for injunctive relief. R. C 192, 228, 275, 335, 365.

On May 2, 1986, the State of Illinois filed a motion for summary judgment, requesting that the court declare the Illinois Tax Act constitutional under both the Illinois and U.S. Constitutions. R. C 654-56. Goldberg and GTE Sprint filed cross-motions for summary judgment, requesting that the tax be declared unconstitutional on the basis of the Commerce Clause. Goldberg also asserted that the tax was void under the Equal Protection Clauses of the U.S. and Illinois Constitutions. R. C 657-59 and

C 728-749; R. C 722-726 and C 755-799.

The trial court ruled against the State of Illinois and in favor of Goldberg and GTE Sprint on their cross-motions for summary judgment. R. C 1044-55; Goldberg J.S. App. E at 18a. The trial court found that the tax triggered Commerce Clause scrutiny, as it taxed interstate phone calling activity, and that it failed three of the four Commerce Clause tests applicable to taxes on interstate activity, as reflected in *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274 (1977). The trial court entered an order, accordingly, adding that there was no just reason to delay an appeal, that its judgment should be stayed, and that its injunction order holding the tax payments in the protest fund should stand until final disposition of the suit. Goldberg J.S. App. E at 19a; R. C 1044-1046.

The State of Illinois appealed directly to the Illinois Supreme Court which reversed the trial court's decision. In doing so, the Illinois Supreme Court agreed with the trial court that the tax was assessed against interstate activity, despite the State's arguments that the tax was a local "sales," "use" or "consumption" tax:

> Under [the Tax Act], the taxable event is the "act or privilege of originating or receiving interstate telecommunications by a person in this state" while the amount of the tax is determined by applying a 5% multiplier to the retail purchase price .... Relying on this statutory language, the Director has applied various designations to the tax in issue. For example, the tax has been denominated as a "purchase tax," "a use tax, i.e. use of [a] privilege," "a tax on the privilege or act of using telecommunications within this State," "a consumption tax," and a tax on the "act, or * * * privilege of consuming messages." However, for purposes of ascertaining whether or not commerce clause analysis applies, it is the taxable event and its practical consequences which are critical rather than the name of the tax or the manner which [sic] the tax is measured. [Citations omitted.] Thus, the fact that section 4 establishes the purchase price of an interstate telecommunication as the basis upon which the tax is calculated does not trans-

> form the taxable event into a retail purchase . . . . Since the taxable event in this case is the "act or privilege of originating or receiving interstate telecommunications * * * in this State," it is clear that the taxable event is linked inextricably to interstate activity -- interstate communication. A person simply cannot make or receive an interstate telecommunication without activating and participating in a complex network of interstate transmissions culminating in interstate communication. We believe that such interstate communication is interstate commerce.

Goldberg J.S. App. C at 9a.

Having decided that the tax is assessed on interstate activity, the Illinois Supreme Court concluded that the tax, to stand, must have sufficient nexus with the taxing state, must be apportioned to activity occurring within the taxing state, must not discriminate against interstate commerce and must bear a fair relation to services provided by the taxing state, under the Commerce Clause tests of *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274 (1977). Goldberg J.S. App. C at 9a-10a and *passim*. In applying these tests, the court held that the Illinois tax failed two of them, *i.e.*, apportionment and discrimination. The court nevertheless concluded that the tax did not violate the Commerce Clause. Goldberg J.S. App. C at 10a. The Court did so by finding, first, that, although *Complete Auto* required apportionment on interstate taxes, "[a]n unapportioned tax . . . is not necessarily invalid," if it avoids imposing a risk of multiple taxation on the same activity. Goldberg J.S. App. C at 11a. As to its finding that the tax discriminates against interstate commerce by imposing actual multiple burdens, the court found that this admitted discrimination was cured by the tax's credit provision, with no discussion or examination of the credit's operation. Goldberg J.S. App. C at 13a.

The court finally found that the tax was fairly related to services provided by the State. The court acknowledged that a disparity existed between the scope of the tax's revenue reach and the extent of services provided by the state as "the State is taxing the 'gross charge' for the entire interstate telecommunication even though the benefits it affords are limited to that portion of the communication occurring within the State." Goldberg J.S. App. C at 13a. Nevertheless, the court found that Illinois hosted "the most critical step in the taxable event -- interstate origination," so that the Illinois tax on the entire charge for the interstate service was "fairly related" to services provided by Illinois. Goldberg J.S. App. C at 13a. The Illinois Supreme Court concluded, in this fashion, that the Illinois tax "passed" all the *Complete Auto* tests and "is [therefore] valid under the commerce clause." Goldberg J.S. App. C at 14a.

E. GTE Sprint Payments under the Tax Act

Under Section 5 of the Tax Act, the ultimate consumers of telecommunications services are liable for payment of the tax, though retailers of those services are held equally liable, whether or not they actually collect the tax. Goldberg J.S. App. F at 30a; Ill. Rev. Stat. ch. 120, § 2005 (1985). From about September 15, 1985 to July, 1986, GTE Sprint paid to the State of Illinois approximately $2,200,000.00 in taxes allegedly due the State under the Illinois Telecommunications Excise Tax. R. C 798. At least $400,000.00 of this amount Sprint paid itself, rather than collecting it from its customers. R. C 798; Sprint J.S. App. C at 10a. As of June 30, 1987, Sprint and its customers had jointly paid into the protest fund approximately $2,431,743.76 in taxes under the Tax Act. R. C 1569-1570 and R. C 1609.

INTRODUCTION AND SUMMARY OF ARGUMENT

A state tax that is imposed on interstate activities must submit to Commerce Clause scrutiny, to assure that the exertion of the state's taxing power will not unduly hinder or impede the free flow of commerce. There could scarcely be a tax more in need of scrutiny under the Commerce Clause than the Illinois tax on interstate telecommunications since such communications represent quintessential and unified interstate activity. But when Commerce Clause scrutiny is applied, it is also apparent that there could scarcely be a tax more deficient in properly limiting the state's taxing powers under the Commerce Clause, as the tax is not fairly apportioned to activity occurring in Illinois, it

discriminates against interstate commerce and it is not fairly related to services provided by Illinois. *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977).

I.

The Illinois tax clearly taxes integral interstate activity. The tax lays a five percent assessment on the entire gross charge for 'originating or receiving' long distance telephone calls in Illinois. Since interstate transmission is the very predicate and concomitant necessity of 'originating or receiving' an interstate telephone call, the object of the tax is interstate calling or transmission activity. This conclusion is so obvious that, in interpreting the tax, both lower courts found that the taxable event under the Tax Act *is* interstate commerce.

Both common law and Commerce Clause construction principles support the state courts' interpretation of the statute. Although the State of Illinois argued that the tax taxes an instate event, such as the local sale, origination, receipt or consumption of the phone call, neither the plain terms of the statute nor the practical effect of the tax support such an interpretation.

First, given the plain meaning of the Tax Act's terms, it cannot be read as a tax on purely local activity. Though the State of Illinois ("State") argued that the tax is a local "sales" tax on the purchase of calls, for example, the only reference to "purchase" in the statute is in a clause, subordinate to the main taxing clause, which identifies the tax base as the gross charge for calls "purchased at retail." But this mere specification of the tax base does not convert the tax on the privilege of engaging in interstate communication into a local sales tax. The Tax Act also clearly states that, although the tax is limited to calls charged to an Illinois address, the tax applies even when calls are billed or paid for outside the state; thus, the tax is assessed even where significant incidents of sale activity occur *outside* the state. Moreover, even if the tax *were* limited to calls "sold" within the state, its practical effect would be to tax interstate call activity. *Central Greyhound Lines, Inc. v. Mealey*, 266 A.D. 648, 44 N.Y.S.2d 652, 654 (App. Div. 1943), *aff'd*, 296 N.Y. 18, 68

N.E.2d 855 (1946), *rev'd*, 334 U.S. 653 (1948); *see also Maryland v. Louisiana*, 451 U.S. 725, 755-56 (1981) (assessing a tax on the sales receipts from interstate activity cannot transform a tax on that interstate activity into a local sales tax).

Neither do the plain terms or practical effect of the tax permit it to be construed as one on the entirely local origination, receipt or consumption of interstate transmission services. The local enjoyment of an interstate transmission cannot exist without the simultaneous use of facilities, network, equipment, and operations that are out-of-state. Thus, Illinois cannot "carve out" of this unified interstate process its allegedly local contacts with it, and claim to be taxing only the latter, because the "local" events are part and parcel of that interstate process. *Michigan-Wisconsin Pipe Line Co. v. Calvert*, 347 U.S. 157, 167 (1954); *Maryland v. Louisiana*, 451 U.S. 725, 754-56 (1981). In sum, the Illinois tax should be construed as taxing interstate activity under applicable construction principles, especially as the origination and receipt of interstate messages has been defined, in other legal contexts, as interstate activity. *Central Greyhound*, 334 U.S. at 659 (definitions in the context of constitutional interpretation should be consistent with treatment in other legal contexts).

II.

Any state tax on interstate activity, including the Illinois tax, must be limited to that portion of the interstate activity that occurs within the taxing state. Such apportionment assures that each state receives only its fair share of revenue from an interstate activity, and prevents unfair burdens arising from more than one state taxing the same or parts of the same activity. *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977). The Illinois tax, however, is in no way related to that portion of interstate calling activity that occurs in Illinois. Instead, Illinois taxes the entire gross charge for the call, despite the fact that other states have contacts with and support such call activity and are also entitled to tax it. Indeed, both state courts below found that the tax is unapportioned -- and precedent from this Court

confirms that such an unapportioned tax laid on the full gross charge for an interstate transmission is invalid. *See Central Greyhound*, 334 U.S. 653, 662-63 (1948).

The State has argued, nevertheless, that the tax is apportioned, being limited to calls either charged in Illinois or involving an Illinois participant. But these limits do not apportion the tax, as application of this Court's recent "internal" and "external consistency" tests for apportionment formulas reveals. *Container Corporation of America v. Franchise Tax Board*, 463 U.S. 159 (1983). For example, under the internal consistency test, a tax must be such that application of a like tax in another state would not result in duplicative taxation. But, if another state imposed a tax like the Illinois tax -- *e.g.*, a tax on long distance calls which originate or terminate and are billed or paid for in this other state -- it is clear that calls between Illinois and this state could be taxed by both. There is no doubt that this other state would have an equal right to assess such a tax because, in its contacts and support of interstate activity, it is indistinguishable from Illinois. Indeed, by taxing the full stretch of calls based on contacts which can be matched by other states on the call's transmission path, Illinois has attempted to *allocate* to itself all effective revenues from the calls, an approach which has met with the disapproval of this Court. *Mobil Oil Corp. v. Commissioner of Taxes*, 445 U.S. 425, 444-46 (1980).

Likewise, the Illinois tax fails the external consistency test for apportionment. External consistency requires that factors used in a tax to divide receipts attributable to instate activity, which is taxable, from receipts attributable to out-of-state activity, which is not taxable, must actually reflect a reasonable sense of how such receipts are generated. *Container*, 463 U.S. 159, 169 (1983). It is uncontested that the gross charge for an interstate call is generated not only by the use and cost of Illinois facilities, but by the use and cost of significant out-of-state network and facilities as well. The Illinois Act simply ignores these other states' contributions to the generation of the call charge or receipts from it, however, because limiting the tax to calls

charged to an Illinois address still does not adequately confine the tax to that portion of interstate calling charge attributable to Illinois transmission activity and costs. The "limits" in the Illinois tax are economically and constitutionally arbitrary ones, insufficient to validate it. The tax therefore fails the external consistency test.

The Illinois Supreme Court recognized that the Illinois tax was unapportioned, but concluded that the tax was constitutional by holding that a tax on interstate activity need not be apportioned if it avoids discrimination. The court's holding was in error, however, ignoring precedent from this Court which demonstrates that (a) though non-discrimination is a necessary condition for the constitutionality of a tax, it is not sufficient; and (b) a tax's failure to apportion constitutes discrimination in itself. In any event, eschewing the apportionment requirement in this case produces a pernicious result, given that states other than Illinois have an equal right to tax their portions of interstate calls. The tax should therefore be invalidated on apportionment grounds.

III.

The Commerce Clause assures free trade among the states and prohibits one state from interfering with the taxing powers of another. Pursuant to this principle, a tax may not discriminate against interstate goods or services, regardless of whether the burden of that discrimination falls on instate or out-of-state consumers. *Boston Stock Exchange v. State Tax Commission*, 429 U.S. 318, 328 (1977); *Bacchus Imports, Ltd. v. Dias*, 468 U.S. 263, 268-69 (1984). However, the Illinois tax seriously discriminates against interstate telephone services in two ways: First, it creates potential and actual multiple taxation of interstate calls, while instate calls are not subject to such a burden and, second, it effectively taxes interstate calling more heavily than intrastate calling.

This Court has recently affirmed that taxes which create even the risk of multiple taxation on the same interstate activity are unconstitutional. *Armco Inc. v. Hardesty*, 467 U.S. 638,

644-45 (1984). The Illinois tax unquestionably poses a risk of multiple taxation. For example, whereas the Illinois tax applies to calls originating or terminating in Illinois and *charged* to a service address there, another state could tax calls originating or terminating there which are *billed or paid for* in that state. Thus, a call made between Illinois and the second state, which is charged to an Illinois address but is billed to or paid by a party in the second state, would be subject to both states' taxes.

Even more significant is the fact that existing taxes in other states, taken together with the Illinois tax, demonstrate that *actual* multiple taxation of long distance calls currently exists. For example, the State of Washington taxes long distance calls originating or terminating there, if the calls are billed or paid for within that state. Consequently, if a call originates in Illinois and is charged to an Illinois address, and terminates in Washington and is billed or paid there, the same call would be taxed by both states (*e.g.*, where a call is made from and charged to an Illinois office of a corporation headquartered in Washington, when headquarters pays the bill). Other states have passed taxes similar to the Washington tax.

Numerous states have also passed taxes on access charges which are the charges long distance carriers pay to the local operating companies for use of local lines to originate or complete interstate calls. Since these portions of interstate transmission represent parts of the same transmission already taxed by Illinois, the taxation by Illinois of the phone call and the taxation by other states of the access charges also constitutes overlapping taxation, even though the two taxes are assessed on different persons or entities. *Telegraph Co. v. Texas*, 105 U.S. 460, 465 (1881) (issue is whether same activity has been taxed more than once, regardless of who bears the burden). The Illinois tax, as applied in conjunction with these other taxes, thus produces multiple taxation of the same call activity. *See* summary of taxes in Appendix A hereto.

Indeed, although the Illinois Supreme Court concluded, erroneously, that the Illinois tax does not create multiple taxation

with regard to calls that *originate* in Illinois -- it acknowledged that the Illinois tax does pose multiple tax burdens on calls that *terminate* in Illinois. This conclusion is sufficient in itself to invalidate the tax. *Armco*, 467 U.S. at 645 ("[i]f another State has taxed the same interstate transaction, the burdensome consequences to interstate trade are undeniable").

The Illinois Supreme Court ultimately upheld the tax, however, by resorting to the tax's credit provision as the supposed "cure" for the tax's admitted apportionment and discrimination ailments. Under the credit provision, a taxpayer subject to two or more taxes on the same calling activity may obtain an Illinois tax credit in the amount of the other state's tax, if the taxpayer demonstrates that it has paid the other state's tax, that the other state's tax was "properly due," and that the other state's tax covered the same activity covered by the Illinois tax. This mechanism fails altogether to apportion the tax and eliminate its discriminatory effect, however.

First, if another state taxes a call taxed by Illinois, and that state tax is less than the absolute amount of the Illinois tax, a taxpayer will continue to pay two states' taxes on the same call, even after the credit, though the Illinois tax will be reduced. This reduction does not eliminate discrimination, however, since the post-credit division of tax between the two states will have no relationship whatsoever to the actual amount of transmission activity which occurs in the two respective states; duplicative taxation persists -- and without apportionment. Indeed, the discrimination effected by the Illinois tax would be eliminated only when the other state's tax *happens* to equal or exceed the amount of the Illinois tax, so that the Illinois tax is entirely cancelled. Such a "cure" is fortuitous and cannot, therefore, validate the tax. *Halliburton Oil Well Cementing Co. v. Reily*, 373 U.S. 64 (1963) (Brennan, J., concurring).

Second, even if the credit could eliminate discrimination, the requirements it places on the taxpayer to do so reintroduce discrimination to the tax. Specifically, a taxpayer subject to two taxes must prove that the other state's tax is "properly due"

and that the two taxes cover the same activity. Given the lack of any criteria for such proofs in the statute, and the fact that such proofs appear to be legal in nature and of a difficulty as to challenge even this Court, the burden placed on the taxpayer to cure the inherent discrimination of the tax constitutes, in itself, a burden on interstate commerce. This is especially true here, where the events taxed constitute pervasive and everyday activity and the need for the credit mechanism will be frequent and great.

The Illinois Supreme Court also suggested that the tax on interstate calls might be defended as non-discriminatory, simply because the Illinois Tax Act places a five percent tax on both inter- and intrastate calls. But, just last term, this Court stated that the Commerce Clause is offended by taxes which, though facially equal, operate to discriminate against interstate commerce. *American Trucking Associations, Inc. v. Scheiner*, 107 S. Ct. 2829 (1987). Here, the Illinois tax, although apparently even-handed, is far from it, for the very reasons cited in *American Trucking*. Specifically, since interstate transmission uses instate facilities with far less frequency than do instate transmissions, an "equal" tax applied to the two falls on the interstate transmissions more heavily. Similarly, the Illinois tax on interstate calls cannot be deemed a tax which compensates somehow for the tax on intrastate calls, because the interstate calls do not involve Illinois services and support to the extent intrastate calls do. The Illinois tax, which falls disproportionately on interstate calling, thus discriminates against interstate commerce, despite the facial equality of the tax. *Maryland v. Louisiana*, 451 U.S. 725, 759 (1981); *Boston Stock Exchange v. State Tax Commission*, 429 U.S. 318, 331 (1977).

IV.

The Illinois tax fails the final *Complete Auto* test because the tax is not related to the services provided the taxed activity by Illinois. Under the fair relation test, the measure of a tax must be reasonably related to the extent of contact the taxed activity has with the taxing state and, in this regard, the incidence of the

tax as well as its measure must be tied to the earnings which the taxing state has made possible. *Commonwealth Edison v. Montana*, 453 U.S. 609, 626 (1981). However, the measure of the Illinois tax is not tied to the earnings or charges that Illinois has made possible with regard to interstate calling. Illinois taxes the entire gross charge for any interstate call, even though it is clear that not all of that charge has been generated by activities within Illinois. In this respect, the Illinois tax strongly resembles the flat privilege tax on inter- and intrastate carriers struck down last term in *American Trucking* where the Court held, as it should here, that a flat tax on the privilege of engaging in interstate and intrastate activities is unconstitutional because the intrastate activity will exercise the privilege accorded by the taxing state fully, while the interstate activity will frequently forego the privilege because it utilizes such privileges intermittently. *American Trucking*, 107 S. Ct. at 2844. Indeed, the Illinois tax is even more insidious than the flat privilege tax in *American Trucking* because the Illinois tax -- being applied to a gross charge which increases the longer a call is and the more it involves interstate activity -- *increases* in amount as the activity which takes place in Illinois *decreases*. There is no doubt, then, that the measure of the Illinois tax is in no way tied to Illinois activity or the earnings which Illinois makes possible. The tax therefore fails the final Commerce Clause test.

ARGUMENT

I. The Illinois Tax Is Applied to Interstate and Not Local Activity, as the Illinois Supreme Court Held

The Illinois Tax Act taxes quintessential interstate activity. The tax "is imposed upon the act or privilege of originating in [Illinois] or receiving in [Illinois] interstate telecommunications." Goldberg J.S. App. F at 29a; Ill. Rev. Stat. ch. 120, § 2004 (1985). Since interstate transmission is the very predicate and concomitant necessity of "originating or receiving" a long distance telephone call, the object of the tax is plainly interstate in nature. Indeed, this conclusion is so apparent that neither court below had any difficulty in construing the taxable event of the

Tax Act as interstate calling activity. Goldberg J.S. App. C at 9a; Goldberg J.S. App. E at 20a-22a. As the Illinois Supreme Court stated:

> Since the taxable event in this case is the "act or privilege of originating or receiving interstate telecommunications * * * in this State," it is clear that the taxable event is linked inextricably to interstate activity -- interstate communication. A person simply cannot make or receive an interstate telecommunication without activating and participating in a complex network of interstate transmissions culminating in interstate communication. We believe that such interstate communication is interstate commerce.

Goldberg J.S. App. C at 9a. This Court should adopt this construction, as it is supported by every relevant state and constitutional rule regarding the construction of taxing statutes.

A. The Illinois Supreme Court's Interpretation of the Taxable Event as Interstate Activity Follows Proper Construction Principles

It is a fundamental canon of statutory construction in Illinois, as elsewhere, that the language of a statute should be given its plain and ordinary meaning. *Franzese v. Trinko*, 66 Ill. 2d 136, 361 N.E.2d 585, 587 (1977). The ordinary meaning of the terms of the Tax Act demonstrate that the taxable event is interstate activity. For example, although the State maintained below that the origination/receipt/use/consumption of interstate calls were discrete, local events which could be fully taxed by Illinois, this assertion defies the ordinary sense of the described taxable event since the "privilege of originating or receiving interstate telecommunications" is utterly dependent upon concomitant interstate transmission activity. Although the sender, receiver or "consumer" of a long distance call may be located in Illinois, his or her initiation, receipt or consumption of the call cannot be divorced from or exist without interstate activities, facilities and transmission. *See* discussion *supra* at 17-18. The local and interstate aspects of the transmission activity are a unified whole.

The plain meaning of the statute also belies the State's assertion below that the taxable event under the Tax Act is the local "sale" of the interstate calling service. The direct object of the main taxing clause in Section 4 is "the act or privilege of originating in [Illinois] or receiving in [Illinois] interstate telecommunications." Goldberg J.S. App. F at 29a. The only reference to "purchase" is not in this main taxing clause, but in a subordinate one, where the five percent multiplier is applied against the "gross charge" for the call, which call is defined as one "purchased at retail." Goldberg J.S. App. F at 29a; Ill. Rev. Stat. ch. 120, § 2004 (1985). The purchase language thus does nothing more than reflect that the tax base will consist of gross charges derived from retail sales.

The definitional portions of the statute positively rebut any reading of the taxable event as a *local* sale, in any event. The statute provides that the five percent multiplier of the tax is to be applied against the "gross charge" for long distance calls, which charge is defined in the statute as "the amount paid" for interstate message services, "amount paid" being subsequently defined as "the amount charged to the taxpayer's service address in Illinois *regardless of where such amount is billed or paid.*" Goldberg J.S. App. F at 25a-26a; Ill. Rev. Stat. ch. 120, § 2002(b) (1985) (emphasis added). A tax is thus assessed against a charge for an Illinois long distance call regardless of whether the charge is billed or paid for in Illinois. Therefore, the tax cannot be deemed "local," even if labeled a "sales tax," because the tax, by its terms, is plainly not confined to sales which occur entirely instate.

B. Commerce Clause Principles Dictate that the State Court's Interpretation of the Taxable Event as Interstate Activity Be Adopted

This Court will defer to the interpretation placed on a state taxing statute by the court of the taxing state, if no reason exists to disapprove it. *United Air Lines v. Mahin*, 410 U.S. 623, 629 (1973). Here, there is every reason for this Court to defer to the Illinois courts' conclusion that the taxable event under the Act is

interstate activity, as such a construction conforms completely to constitutional principles applicable to the interpretation of state taxing statutes.

1. The Practical Effect of the Tax Is To Tax Interstate Calling Activity

In evaluating taxes under the Commerce Clause, this Court has consistently held that it is the practical and economic effect of the tax which governs the determination of whether the tax is interstate in nature, so as to trigger constitutional scrutiny. *Maryland v. Louisiana*, 451 U.S. 725, 756 (1981) (the "practical operation" of a tax controls in assessing its constitutionality); *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 288-89 (1977); *Halliburton Oil Well Cementing Co. v. Reily*, 373 U.S. 64, 69-70 (1963). Here, it is clear that the Illinois courts correctly adhered to this principle, in construing the taxable event under the Illinois tax as interstate activity. As the trial court aptly stated:

> [T]he state asks the Court to focus on one-half of what goes on during [an interstate phone call], that is, the originating or receipt of a phone call....
>
> * * *
>
> To my view it strains both common knowledge and common sense to characterize an interstate phone call in terms of an Illinois sale at retail and thereby *ignore the realities* of its interstate participant and the interstate communication system over which it has taken place.

R. C 1048-1049, C 1050; emphasis added. Likewise, the Illinois Supreme Court relied on the practical thrust of the tax:

> Thus, the fact that section 4 establishes the purchase price of an interstate telecommunication as the basis upon which the tax is calculated does not transform the taxable event into a retail purchase which, by definition, is local.... Since the taxable event in this case is the "act or privilege of originating or receiving interstate telecommunications * * * in this State," it is clear that the taxable event is linked inextricably to interstate activity -- interstate communication. A person simply cannot make or receive an interstate telecommunication without activating and participating in a complex network of interstate transmissions....

Goldberg J.S. App. C at 9a.

This Court's analysis of the practical effect of taxes similar to the Illinois tax demonstrates that the courts below were correct in these holdings. For example, this Court has refused to deem taxes "local" by focusing on the taxpayer, rather than on the subject of a tax. In *Telegraph Co. v. Texas*, 105 U.S. 460 (1881), the Alabama state court had construed a tax as a constitutionally valid, local "occupation" tax on a telegraph company that sent and received interstate messages. However, since the tax was assessed as a percentage of receipts for all messages transmitted or received, this Court concluded that, as a practical matter, the tax fell on the interstate message activity itself, not on the local occupation of the telegraph company, holding:

> [W]here the burden of a tax falls on a thing which is the subject of taxation, the tax is to be considered as laid on the thing rather than on him who is charged with the duty of paying it into the treasury....

105 U.S. at 465. Similarly, the Illinois Tax Act, as drafted, is assessed on gross charges for interstate calling activity, and the burden of the tax clearly falls on that interstate calling activity rather than any local activity of the taxpayer.[6]

This Court has also refused to deem taxes local in nature by isolating and focusing on some discrete aspect of interstate activity which is part of a unified and continuous interstate flow. For example, in *Michigan-Wisconsin Pipe Line Co. v. Calvert*, 347 U.S. 157, 167 (1954), an interstate gas pipeline operator challenged an "occupation" which was tax levied on

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[6] As the trial court found:

> *The relevant inquiry is* as to just *what is being taxed and not who is* being taxed and when that inquiry is made as to these calls, it is apparent that what is being taxed is the interstate phone call.

Goldberg J.S. App. E. at 21a; emphasis added.

the "...'taking' [of gas stored within the State] into [the taxpayer's] pipelines ... solely for interstate transmission ...," and that was assessed on the entire volume of the gas to be transmitted. Although the State maintained that the statute should be construed as taxing the *wholly instate loading* of the gas into the interstate pipeline, this Court, looking to the practical effect of the tax, disagreed, concluding that a mere "aspect of interstate transportation" cannot be "carve[d] out [for local taxing] from what is an entire or integral economic [interstate] process ... [t]he separation must be realistic. ... " 347 U.S. at 166, 169. *Accord Maryland v. Louisiana*, 451 U.S. 725, 754-56 (1981) (tax on "first use" or processing of natural gas brought from outside the state taxed the interstate flow of gas, even though local events might interrupt it). Similarly, the mere origination or termination in Illinois of a unified interstate transmission cannot transform a tax on that activity into a local one.

This Court has also refused to view a tax on interstate services as taxing a local event simply because sales receipts from the provision of those services are collected in the taxing state. Contrary to the State's argument below, the Illinois tax is not one which is limited to calls purchased or receipts collected in Illinois, since the tax covers calls regardless of whether such calls are billed or paid for in Illinois. However, even if the Illinois tax *were* so limited, it still could not be deemed a tax on purely local activity. For example, *Central Greyhound Lines, Inc. v. Mealey* involved a New York tax on gross receipts collected by a bus company for transportation between two points within the state but partially routed through New Jersey and Pennsylvania. This Court treated the tax as applied to interstate activity, even though the transportation began and ended and the receipts for the same were collected within the taxing state. *Central Greyhound*, 266 A.D. 648, 44 N.Y.S.2d 652, 654 (App. Div. 1943), *aff'd*, 296 N.Y. 18, 68 N.E.2d 855 (1946), *rev'd*, 334 U.S. 653 (1948).

Similarly, in *Western Union Telegraph Co. v. Alabama State Bd. of Assessment*, 132 U.S. 472 (1889), the Alabama Supreme

Court had construed a tax on gross receipts from interstate telegraph and telephone message services as taxing only local activity because "all receipts derived from business done in the State, [are] *actually received there*, though the message may have been delivered at, or may have been sent for delivery from, some office out ... of the State." 132 U.S. 472, 474 (1889) (emphasis added). This Court reversed, holding that the tax was laid "upon receipts properly appurtenant to interstate commerce," and so constituted a tax on interstate activity. 132 U.S. at 476. *Accord Maryland v. Louisiana*, 451 U.S. 725, 755-56 (1981) (fact of sale within the state does not convert activity involving interstate flow into local event, for Commerce Clause purposes, citing *Illinois Natural Gas Co. v. Central Illinois Public Service Co.*, 314 U.S. 498, 503-504 (1942)). Likewise, here, the Illinois tax, even if it were limited to receipts *collected* or services *purchased* in Illinois, must be deemed a tax on interstate activity.

2. The Subject of the Tax Should Be Considered Here, as Elsewhere, Interstate Activity

The activity taxed by the Illinois Tax Act has been consistently treated as interstate commerce in the context of other legal relations. For example, the taxed calling activities have been generally deemed common carrier services subject to Federal Communications Commission regulation, because they constitute "interstate commerce."[7] To treat the taxed activity here

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[7] *Cf. Idaho Microwave, Inc. v. F.C.C.*, 352 F.2d 729, 732 (D.C. 1965) (Common carrier of microwave transmissions service sought to avoid requirements under statute, under exemption for *intrastate* communication service. Carrier maintained it qualified for exemption because its facilities were all located in one state. The court rejected the argument, noting that, though the carrier's facilities were located in one state, its service was to provide communications among different states and, even if conducting merely an instate relay, service must be deemed "interstate commerce"). *See also Ward v. Northern Ohio Telephone Co.*, 300 F.2d 816, 819 (6th Cir.), *cert. denied*, 371 U.S. 820 (1962) (Federal Communications Act requires telephone companies to furnish

(Footnote continued on the following page)

differently, then, for constitutional purposes, would violate this Court's teaching in *Central Greyhound Lines, Inc. v. Mealey* that: "[t]o label [activity] across [state lines] 'local commerce' for some purposes when it is 'interstate commerce' in other relations . . . is to use loosely terms having connotations of constitutional significance. * * * Especially in the disposition of constitutional issues are [such] legal fictions hazardous, because of the risk of confounding users and not merely readers." 334 U.S. 653, 659 (1948). To avoid such a hazard, activity taxed by Illinois under the Tax Act should be considered here, as elsewhere, interstate commerce.

II. The Illinois Tax on Interstate Calling Activity Violates the Commerce Clause

This Court has long viewed the Commerce Clause not only as a grant of Congressional power over interstate activities and instrumentalities, but also as a limit on the states' power to interfere with such activities and entities. *American Trucking Associations, Inc. v. Scheiner*, 107 S. Ct. 2829, 2838 (1987). In order to assure that the exertion of state taxing power will not unduly hamper the flow of interstate commerce, the Court has thus required that state taxes on interstate activity be assessed (a) only on that portion of the activity which occurs within the taxing state; (b) in a manner which avoids discrimination against interstate commerce; and (c) so as to fairly relate the tax to services provided by the taxing state. *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977); *see also Maryland v. Louisiana*, 451 U.S. 725, 754 (1981). The Illinois tax on interstate activity meets none of the foregoing three requirements.

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7 *(continued)*

wire service to radio stations. The telephone company here refused to do so, on the ground that it was not in interstate commerce, as its facilities were located instate. The court rejected this position because the telephone lines were to be used for the (instate) beginning and end of the interstate transmission: in "furnishing . . . [of] wires for broadcast purposes, [the phone company] is engaged in interstate commerce").

A. The Tax Violates the Commerce Clause because It Is Not Apportioned

1. The Tax Is Not Apportioned to Activity Occurring within Illinois

To pass Commerce Clause inspection, a tax on interstate activity must be apportioned to that segment of the interstate activity which occurs within the taxing state. *Armco Inc. v. Hardesty*, 467 U.S. 638, 644 (1984); *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977); *Central Greyhound Lines, Inc. v. Mealey*, 334 U.S. 653, 662-63 (1948). The Illinois tax, however, is not even purportedly limited to that portion of interstate calling activity which occurs in Illinois. Instead, the Illinois tax taxes the entire gross charge for an interstate call, even though the charge is generated in part by significant activities outside the state. As the Illinois Supreme Court found, "[s]ince the instant tax applies to the entirety of [the gross charge for] each and every interstate telecommunication, it is not an apportioned tax." Goldberg J.S. App. C at 10a (emphasis added).

Applicable precedent confirms the tax is unapportioned. In *Central Greyhound Lines, Inc. v. Mealey*, 334 U.S. 653, 662-63 (1948), this Court held that the New York tax laid on gross receipts from interstate bus transportation would be void under the Commerce Clause, unless it were limited to the percentage of the gross receipts equal to that proportion of the total multistate transportation mileage that occurred in New York. The unapportioned Illinois tax at issue here is likewise invalid because it is in no way limited to a percentage of the interstate call charges which corresponds to that portion of interstate telephone transmission activity occurring in Illinois.

2. The Tax Does Not Include a Formula or Method for Apportionment

Recent discussion of apportionment by this Court underscores the invalidity of the Illinois tax. In *Container Corporation of America v. Franchise Tax Board*, 463 U.S. 159 (1983), the Court examined a corporate franchise tax which was applied to income from "unitary" interstate business and which included an

apportionment formula for determining that segment of income which could constitutionally be attributed to -- and therefore taxed by -- the taxing state. The Court held that the formula, to be valid, must be "fair," that is, it must possess "internal" and "external consistency:"

> [Where a tax is applied to interstate activity] a State must . . . apply a formula apportioning the income of that business within and without the State. Such an apportionment formula must, under both the Due Process and Commerce Clauses, be fair. [Citations omitted.] The first, and again obvious, component of fairness in an apportionment formula is what might be called internal consistency -- that is, the formula must be such that, if applied by every jurisdiction, it would result in no more than all of the unitary business' income being taxed. The second and more difficult requirement is what might be called external consistency -- the factor or factors used in the apportionment formula must actually reflect a reasonable sense of how income is generated.

Container, 463 U.S. at 169. Examining the Illinois tax, it is clear that the tax contains no formula which even vaguely meets these apportionment criteria.

a. The Tax Contains No Apportionment Formula under the Internal Consistency Test because Like Taxes Allow Duplicative Taxation of the Same Calls

Container requires that the apportionment formula of a tax on unified interstate activity be such that, if applied by other states, it would not result in the taxed activity being taxed more than once. In *Armco Inc. v. Hardesty*, this Court more recently applied this "internal consistency" test to a gross receipts tax on interstate activity, by inquiring whether the imposition by another state of a "*like* tax," with a like formula, would result in the activity being taxed by more than one state. 467 U.S. 638, 644-45 (1984) (emphasis added) (citing *Halliburton Oil Well Cementing Co. v. Reily*, 373 U.S. 64, 72 (1963) (testing a tax by

calculating effect if "*similar* . . . tax structures were adopted in other states")).

Applying this test, it is clear the Illinois tax is not apportioned. If a tax "like" the Illinois tax, *i.e.*, one on calls originated or received in a state, were enacted in other states, then more than one state could tax a long distance call. For example, Illinois taxes the gross charge for long distance calls originating or terminating there. However, the taxing state on the opposite end of the call could, under this same tax, tax the activity already taxed by Illinois. And, since Illinois taxes the entire gross charge for the call, the other state's tax would perforce result in duplicative or overlapping taxation. There are many other conceivable like taxes which would work the same result. *See* discussion *infra*, at 34-38. The Illinois tax therefore fails the internal consistency test.

The State maintained below that the Illinois tax did possess internal consistency since, if every state were to apply a tax *identical* to the Illinois tax -- that is, on long distance calls originating or terminating and "purchased" in the taxing state -- only one state could tax each long distance call, *i.e.*, the state of purchase. This argument totally misapprehends the apportionment concept and the role of "internal consistency."[8] For example, if every state passed a tax *identical* to the Illinois tax, it is true only one state would tax a long distance call (*i.e.*, the "charging" state) but, then, other states which host and economically support significant transmission, billing and purchase activity on that call would be deprived of revenues based on those activities. *See* Statement of the Case at 3-4. There would simply be no apportionment of the tax among the states where substantive interstate transmission or calling activity occurs, even though there might be no technical tax overlap.

Indeed, the approach the State espouses is nothing more

[8] The State's argument is also premised on the false assumption that the Illinois tax is limited to calls purchased in Illinois. It is not. The Illinois tax is limited to calls charged to an Illinois service address, but is applied even where calls are billed or paid for in other states.

than an arbitrary allocation of all revenues from an interstate activity to one state having partial contact with it. However, just recently, this Court frowned upon interstate taxation by allocation -- precisely because awarding exclusive power to one state to tax interstate activity deprives other states supporting that activity of their fair share of revenues. *Mobil Oil Corp. v. Commissioner of Taxes*, 445 U.S. 425, 444-446 (1980); *Container*, 463 U.S. 159, 164 (1983).[9] In *Mobil Oil*, the Court further suggested that the allocation approach is problematic, inasmuch as endorsing it could be tantamount to proscribing apportionment altogether, since an apportionment formula (applied by one state) would operate together with an allocation formula (applied by another) to produce forbidden multiple taxation. *Mobil Oil*, 445 U.S. at 444-46. Endorsement of a true apportionment formula, by contrast, is far preferable because it provides the states with latitude to draft different types of taxes on interstate calling activity, allows all states having contacts with the calling activity to obtain a share of revenues from it, and automatically prevents each state from seriously encroaching on the taxing territory of the other, guaranteeing an area of free trade among the states. *Boston Stock Exchange v. State Tax Commission*, 429 U.S. 318, 328 (1977).

An "apportionment" test which cares only for avoiding technical duplicative taxation is not enough, then, because such a litmus test does not prevent one state from interfering with the taxing powers of another. Illinois has no right to tax the full stretch of interstate calls beginning and ending there because there are other states which have equal substantive contacts

[9] The Court in *Mobil Oil* went so far as to state that there is little reason for taxation by allocation, even in its traditional context, *i.e.*, taxation of intangible property. *Mobil Oil*, 445 U.S. at 444-445. Indeed, the states have largely rejected the allocation approach in taxing income from sales of interstate manufacturing (for example), opting, instead, for either apportionment or separate accounting approaches. W. Hellerstein, *State Income and Taxation*, 79 Michigan L. Rev. 113, 116-17 (1980) (and sources cited therein).

with those calls. And its rights are not improved by its having been first to do so. As Justice Goldberg commented in his dissent to *General Motors Corp. v. Washington*, 377 U.S. 436, 458 (1964), "[p]resumably, if there is to be a limitation on the taxing power of each . . . [state], that limitation surely cannot be on a first-come-first-tax basis." The more reasoned and better test is the application of *like* taxes, as recommended in *Armco*, which recognizes that state contacts with interstate activity may appear to differ, yet be "like" in the sense that they provide an equal and similar basis for a tax -- and that this must be taken into the constitutional "duplicative taxation" account.

Applying taxes "like" the Illinois tax in other states, then, it is apparent that more than one state can tax the interstate calling activity taxed by Illinois. For example, other states have already passed taxes that cover calls which originate or terminate within their boundaries and which are, in some manner, billed or paid there.[10] The billing contacts on which these types of taxes are based are substantively the same as the charge contact used by Illinois, so the taxes are highly similar to the Illinois tax. But imposition of these similar taxes results in multiple taxation of calls between Illinois and these states because calls which are *charged* to an Illinois address but are *billed or paid* for in these other states may be taxed by both Illinois and these other jurisdictions. The Illinois tax thus fails the internal consistency test, as correctly applied.

b. The Tax Contains No Apportionment Formula under the External Consistency Test because It Covers the Full Gross Charge for Calls, though Much of that Charge Is Generated by Costs and Economic Activity Outside the State

The Court's holding in *Container* also requires that a tax on interstate activity pass what it termed the "external consis-

[10] *See* taxes imposed, *e.g.*, by Arkansas, New Mexico, Ohio, and Washington, as cited in Appendix A hereto.

tency" test. To have external consistency, the factors used in the tax to divide income attributable to instate activity, which is taxable, from income attributable to out-of-state activity, which is not taxable, "must actually reflect a reasonable sense of how [the tax base] is generated." *Container Corporation of America v. Franchise Tax Board*, 463 U.S. 159, 169 (1983). However, uncontested evidence shows that the gross charge for an interstate call is generated not only by the use and cost of Illinois facilities, but by the use and cost of significant out-of-state network and facilities as well. *See* Statement of the Case at 3-4. The Illinois tax is nevertheless assessed against the entire gross charge for a long distance call, there being no attempt to divide the gross charge, according to a realistic sense of how it is generated, between instate and out-of-state activity. As a consequence, the Illinois tax has no "external consistency," and is unconstitutional under *Container*, for failure of apportionment.

Despite this failure, the State argued below that the tax *was* apportioned because (a) the tax is limited to calls that are charged to an Illinois service address, and (b) the tax is limited to calls involving an Illinois purchaser of or participant in the interstate call. Neither of these arguments is tenable under the external consistency test, however. For example, the limit of the tax to calls charged to an Illinois address in no way segregates out and taxes that portion of Illinois transmission activity and costs involved in a long distance call, while protecting substantial non-Illinois transmission activity and costs from taxation. If a call originates in Illinois and is charged to an address there, Illinois taxes the entire gross charge for the call, regardless of the substantial economic support provided the call by the other state(s) on the call's transmission path. The Illinois charge limit is therefore an economically arbitrary limit on the tax, insufficient to apportion and validate it. *Central Greyhound Lines, Inc. v. Mealey*, 266 A.D. 648, 44 N.Y.S.2d 652, 654 (App. Div. 1943), *aff'd*, 296 N.Y. 18, 68 N.E.2d 855 (1946), *rev'd*, 334 U.S. 653 (1948) (New York tax on interstate bus transportation deemed objectionable even though the tax was limited to those receipts collected by the bus company in New York).

As to the argument that the Illinois tax is apportioned because limited to calls involving an Illinois participant or purchaser, the same reasoning applies. Confining the tax to those calls involving an Illinois participant or caller would still not identify that percentage of instate transmission activity and costs involved in each long distance call, and confine the Illinois tax to the corresponding percentage of the call's gross charge. Therefore, the State's arguments are misdirected, and the tax utterly fails the external consistency test.[11]

3. The Unapportioned Tax Cannot Be Valid under the Commerce Clause because Its Failure To Apportion Constitutes Discrimination

The Illinois Supreme Court rejected the State's argument that the Illinois tax is apportioned. Goldberg J.S. App. C at 4a. It nevertheless upheld the tax on the ground that apportionment of a tax is not required, as long as it otherwise avoids discrimination. That conclusion was inconsistent with this Court's decisions in two respects. First, in *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977), this Court expressed the Commerce Clause tests for taxes on interstate activity in the conjunctive; hence, the apportionment test cannot be simply eliminated. Second, this Court has held that the failure of a tax to apportion itself to instate activity itself portends prohibited discrimination. *Armco Inc. v. Hardesty*, 467 U.S. 638, 644 (1984) ("A tax that unfairly apportions income from other States is a form of discrimination against interstate commerce").[12]

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[11] Indeed, it is not certain that either an Illinois participant or purchaser will be involved in all calls taxed by Illinois. A taxed call could, for instance, be charged to an Illinois address and still not involve a participant in Illinois, if the call were charged by card. Further, as already shown, the taxed calls are not necessarily billed or paid for in Illinois.

[12] This Court has suggested elsewhere that one of the Commerce Clause tax tests cannot substitute for another. *Westinghouse Electric Corp. v. Tully*, 466 U.S. 388, 399 (1984). It appears, then, that nondis-

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Furthermore, the Illinois court advanced no tenable argument for dismissing the apportionment requirement, as its flawed reasoning and citation of inapposite precedent demonstrate. For example, the court's reliance on *Wisconsin Telephone Co. v. Wisconsin Department of Revenue*, 125 Wis. 2d 339, 371 N.W.2d 825 (Ct. App. 1985), in which the court analyzed a tax on long distance messages and found apportionment unnecessary, was misplaced. In *Wisconsin Telephone*, the state court had construed the tax on long distance calls at issue as a tax on the local sale of such calls. Since the tax was deemed local, the court concluded that apportionment was irrelevant. *Wisconsin Telephone*, 371 N.W.2d at 830. The Illinois court, by contrast, construed the Illinois tax as applied not to a local event, but to *interstate* activity, where apportionment is clearly necessary. The Illinois court thus erred by adopting the Wisconsin court's conclusion while rejecting the very premise upon which that conclusion rests.[13]

The Wisconsin Court's theory that apportionment is optional under the Commerce Clause has also been the subject of attack in recent analysis undertaken here. For example, the Wisconsin court relied heavily on this Court's validation of an unapportioned gross receipts tax in *General Motors Corp. v. Washington*, 377 U.S. 436 (1964), in concluding that an unapportioned tax is not *per se* unconstitutional. *Wisconsin Telephone*, 371 N.W.2d at 830. However, given this Court's recent disapproval of *General*

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12 *(continued)*

crimination is a necessary but not sufficient condition of a constitutional tax, contrary to what the Illinois Supreme Court held.

[13]The Wisconsin court's finding that this tax was assessed on local activity was in error, in any event. *See* discussion *supra* at 17-24. Even so, that finding also rested on the Wisconsin court's assumption that only one state's tax could ever be applied to a bill for a call. However true that may have been with regard to the Bell Operating Company involved there, GTE Sprint, by contrast, has the capability of billing more than one state's tax on one bill for the same phone call. *See* Statement of the Case, *supra* at 4 and discussion *infra*. *Cf. Wisconsin Telephone*, 371 N.W.2d at 830.

Motors and its reliance on the dissenting opinion, the *dicta* in *General Motors*, to the effect that an unapportioned tax may be constitutional, is highly suspect. *See Armco Inc. v. Hardesty*, 467 U.S. 638, 642 (1984); *Tyler Pipe Industries, Inc. v. Washington State Dept. of Revenue*, 107 S. Ct. 2810, 2816 (1987). *See also General Motors*, 377 U.S. at 450 (Brennan, J. dissenting, objecting to short shrift given to apportionment requirement). Recent developments in Commerce Clause state tax analysis appear to have fairly vitiated the force of *General Motors*, then, and suggest that, by eschewing the apportionment requirement, the Wisconsin and Illinois courts erred.

In sum, neither the Wisconsin decision, nor the *General Motors* case upon which it relied, present compelling authority for dismissing the apportionment requirement.[14] Further, as the facts show, dispensing with the apportionment requirement with regard to the tax at issue here would lead to pernicious results. Therefore, the Illinois tax, which is clearly unapportioned, should be struck down.

B. The Tax Violates the Commerce Clause because It Discriminates against Interstate Commerce

The purpose of the Commerce Clause is to create and protect free trade among the states. *Boston Stock Exchange v. State Tax Commission*, 429 U.S. 318, 328 (1977) (as cited in *Armco Inc. v. Hardesty*, 467 U.S. 638, 642 (1984)). In light of this purpose, a fundamental Commerce Clause principle is that no state may impose a tax which discriminates against interstate commerce by providing an advantage to instate interests. *Maryland v. Louisiana*, 451 U.S. 725, 754 (1981). This principle pro-

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[14]The Wisconsin court also simply rejected or ignored the applicable multiple burden discrimination test set out in *Armco Inc. v. Hardesty*, 467 U.S. 638, 644 (1984). Since the state court relied, in part, upon its finding of no multiple burdens to dispense with the apportionment requirement, its analysis is even more questionable. *Wisconsin Telephone*, 125 Wis. 2d 339, 371 N.W.2d at 830.

hibits discrimination against interstate services, regardless of where the burden for such discrimination falls. *Bacchus Imports, Ltd. v. Dias*, 468 U.S. 263, 268-269 and n.8 (1984) (the Commerce Clause is violated even if instate and out-of-state taxpayers equally bear the brunt of discrimination against out-of-state products).

The Illinois Tax Act seriously discriminates against interstate calling activity or service in two ways. First, it creates potential and actual multiple taxation of the same interstate calling activity by Illinois and other states, while purely intrastate calling activity is not exposed to such multiple burdens. Second, the Illinois taxing scheme effectively taxes interstate calling more heavily than intrastate calling. Regardless of the validity of the Illinois Supreme Court's holding on apportionment, then, its decision that the tax is constitutional requires reversal, because the tax illegally discriminates against callers who call outside the state.

1. The Tax Discriminates by Imposing Multiple Burdens on Interstate Calls

a. The Tax Creates the Risk of Multiple Taxation

Taxes that create even a risk of multiple taxation on the same interstate activity are discriminatory and impermissibly burden interstate commerce. *Western Live Stock v. Bureau of Revenue*, 303 U.S. 250, 255-56 (1938); *International Harvester Co. v. Department of Treasury*, 322 U.S. 340, 360 (1944) ("the risk of multiple taxation creates the unconstitutional burden which actual taxation by [more than one state] would impose in fact"). This Court has recently reiterated and reinforced its position that a tax on interstate activity is void if hypothetical, "like" taxes could be imposed by other states on the same activity. *Armco Inc. v. Hardesty*, 467 U.S. 638, 644-45 (1984); *Westinghouse Electric Corp. v. Tully*, 466 U.S. 388 (1984).

Applying *Armco*, it is clear that the Illinois tax creates an impermissible risk of multiple taxation. The Illinois tax is applied to the total charge for the act or privilege of originating

or receiving an interstate call in Illinois, if the call is charged to an Illinois service address. But another state, let us say "New York," might pass a "like" tax on interstate calls originating or terminating and billed or paid for there. If a call were made from Illinois to New York, then, Illinois could tax the call because it begins in Illinois and could be charged to an Illinois address, but New York could also tax the call because the call terminates in the State of New York and the call, though charged to an Illinois address, might be either billed or paid for in New York.[14] As a consequence, the application of this hypothetical New York tax, together with the Illinois tax, results in multiple taxation of the same call. Such a risk of multiple taxation would be even greater if the hypothetical state's tax were not limited to calls paid or billed locally. Under the *Armco* hypothetical risk test, then, the Illinois tax is unconstitutional.

b. The Tax Creates Actual Multiple Taxation

Although a showing of actual multiple taxation of the same activity is not necessary to invalidate a tax on that activity under the Commerce Clause, such a showing surely dooms it. *See American Trucking Associations, Inc. v. Scheiner*, 107 S. Ct. 2829, 2841 (1987). As this Court has stated, "[i]f another State has taxed the same interstate transaction, the burdensome consequences to interstate trade are undeniable." *Armco Inc. v. Hardesty*, 467 U.S. 638, 645 n. 8 (1984). Here, it is undeniable that the Illinois tax unduly burdens interstate commerce since jurisdictions other than Illinois are already applying *actual* taxes on the very calls taxed by Illinois.

Several states and municipalities have levied taxes on interstate telecommunications services which, when combined with the Illinois tax, produce multiple taxation of the same activity.

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[14] For example, a call might be *charged* to a phone at the Illinois division of a New York corporation, but the bill *paid* at corporate headquarters in New York.

As examples:[15]

(1) The State of Washington imposes a tax on the "privilege" of engaging in interstate phone calls. Wash. Rev. Code Ann. §§ 82.04.065 and 82.04.250 (Supp. 1988); Sprint J.S. App. G at 17a-19a. Washington's tax is applied to the gross proceeds from all long distance calls originating or terminating in that state, when such calls are billed or paid for there. As a consequence, a long distance call from Illinois to Washington and charged to an Illinois address, but billed or paid for in Washington, could be taxed by both Illinois and Washington. A number of other states have passed taxes on long distance calls similar to the Washington tax, which taxes cover calls originating or terminating and billed in the state, in some manner (*e.g.*, billed to an instate customer or user (Arkansas, Florida, Oklahoma); to an instate telephone number (Arkansas, New Mexico, Ohio, Texas); to an instate telephone (Minnesota); or to an instate account (New Mexico, Ohio)). *See* citations to and summary of these statutes in Appendix A hereto. The imposition of any of these taxes, together with the Illinois tax, results in duplicative taxation of the calls between Illinois and these states since Illinois taxes calls even when they are billed elsewhere.

(2) A Los Angeles, California Ordinance applies a tax to every person in the City of Los Angeles using and (apparently) paying for interstate telephone communication services in the City. Los Angeles, Cal., Ordinance No. 162586 (July 7, 1987). *See* App. D hereto. A call between Illinois and Los Angeles could thus be taxed by both if the call were charged to an Illinois service address and paid for in Los Angeles, as, for example, where a call is made and charged to an Illinois office of a business headquartered in Los Angeles, and the phone bill is paid at

[15] In its Jurisdictional Statement, GTE Sprint used taxes from the City of Wheat Ridge and the City of Greeley, Colorado in its multiple burden discussion. Since that time, these two taxes have been amended. The full text of the taxes, as amended, have been reprinted in the Appendices hereto as Appendix E and F.

headquarters.

(3) A number of other states have also imposed a tax similar to the Illinois tax on long distance calls, by imposing a tax on charges for "access service."[16] A charge for "access service" is a charge local carriers assess against interstate carriers for the privilege of allowing the interstate carriers to originate or terminate their interstate transmissions at the local level. *See* Statement of the Case at 4; Sprint J.S. App. C at 8a. Such services and charges are necessary and integral portions of the activity already covered by the Tax Act, as the Act itself states.[17] Therefore, taxes on access charges and the Illinois tax are "like" taxes, covering the same transmission activity. The concomitant existence of the access charge taxes and the Illinois Tax Act clearly produces actual, multiple taxation, however. To illustrate: The Illinois tax is assessed against the total charge for an entire interstate call originating in Illinois and charged to a service address in Illinois. If a call therefore originates in Illinois and terminates in Wisconsin -- where a tax on access charges is assessed -- Illinois will tax the consumer on his charge for the total interstate transmission while Wisconsin will tax the carrier on the access charge paid for the local transmission necessary simply to complete the very same call. Thus, when calls are made between Illinois and Wisconsin (or another state with

[16] Transaction, sales and/or use taxes are imposed by the following states upon charges for "access services:" Colorado, Colorado Emergency Retail Sales Tax Act of 1935, Colo. Rev. Stat. § 39-26-104(1)(c) (1982), interpreted in Revenue Bulletin 83-7, October 1983 (see App. C hereto) (imposes tax on interstate access charges); Michigan, *see MCI Telecommunication Corporation v. State of Michigan*, 136 Mich. App. 28, 355 N.W.2d 627 (1984) (use tax applies to purchase of access services by interstate carrier); Wisconsin, Wisconsin General Retail Sales Act, Wis. Stat. Ann. § 77.51(14) (m) (West Supp. 1987) (sales tax imposed upon transfers of services permitting the origination and termination of telephone messages). *See* App. A hereto.

[17] The Illinois Tax Act acknowledges that these services are integral parts of the taxed end-to-end interstate communications. Ill. Rev. Stat. ch. 120, § 2002(c).

an access charge tax), at least one end of the telephone transmission can be taxed twice, though the tax may be assessed on different taxpayers.[18]

The imposition of these various sales, privilege and access charge taxes, together with the Illinois tax, can and do bring about multiple taxation of the same calling activity. Under the Illinois Tax Act, Illinois has taxed the full stretch of an interstate transmission. But other states inevitably involved in the transmission of the same interstate call have a right equal to Illinois to assess taxes on their own instate portions of it, whether that entails the origination or receipt of the call, the partial transmission of the call, or aspects of its sale (*e.g.*, "billing and payment"). As a consequence, the Illinois tax creates actual multiple burdens anytime any one of these other states also imposes a tax -- no matter how limited -- on the same transmission.

The Illinois Supreme Court's reasoning in dismissing the multiple taxation problem posed by the Tax Act represents a serious misunderstanding of both the operation of the tax and precedent from this Court. For example, the Illinois court found that, with regard to those communications which *originate* in Illinois, no risk of multiple taxation exists. Goldberg J.S. App. C at 11a. But there is absolutely no evidence in the tax or the record -- nor none cited by the court -- which would support this conclusion. Indeed, to the contrary, GTE Sprint has submitted uncontested evidence here and below, in the form of actual taxes, establishing that the Illinois tax operates to impose multiple burdens on the calls taxed by Illinois, whether they begin or

[18] To the extent that the access charge taxes are assessed against the carriers, while the Illinois tax is assessed on consumers, this Court held long ago that the pertinent inquiry is whether or not the same *activity* is subject to multiple taxation, regardless of whether one or more persons or entities bear the burden of it. *Telegraph Co. v. Texas*, 105 U.S. 460, 465 (1882); *see also Maryland v. Louisiana*, 451 U.S. 725, 756-757 (1981). Furthermore, under the Illinois tax, the carriers are made equally liable for the tax, in any event, so that a carrier in Illinois *could* be liable for both taxes. *See* Statement of the Case at 9.

end in Illinois. *See* discussion *supra* at 36-38 and tax summary in App. A hereto.

Indeed, rather than examining the actual effect of the Illinois tax, the Illinois Supreme Court relied almost entirely on recent Wisconsin and Alaska state court cases upholding interstate telephone call taxes to support its position that calls originating in Illinois cannot be subject to multiple taxation. *See* Goldberg J.S. App. C at 11a; *Douglas v. Glacier State Telephone Co.*, 615 P.2d 580, 588 (Alaska 1980) ("*Douglas*"); *Wisconsin Telephone Co. v. Wisconsin Department of Revenue*, 125 Wis. 2d 339, 371 N.W.2d 825, 830 (Ct. App. 1985) ("*Wisconsin Telephone*"). These state courts' conclusions are not relevant to the issue of whether the Illinois tax is valid, however, for two reasons.

First, the Alaska court and Wisconsin court each construed its state's tax on long distance phone calls as a local "sales" tax and reasoned, therefore, that only one state (itself) could assess a tax on that local "sale." By contrast, the Illinois court found that the Illinois tax is *not* a tax on a local sale, but a tax on interstate calling activity. Goldberg J.S. App. C at 8a-9a. The Wisconsin and Alaska court decisions in no way support the Illinois court's conclusion, then, given the Illinois court's broader interpretation of its state's tax.

Second, the Alaska and Wisconsin courts assumed that their "sales" taxes could never create the possibility of multiple taxation on the same call, since, they surmised, only one bill with one tax would be sent to any one entity on a call. *Wisconsin Telephone*, 371 N.W.2d at 830. However, the Illinois tax taxes interstate calls which begin or end in Illinois and which are charged to an Illinois service address, *regardless of where they are billed or paid*. The Illinois tax applies, then, to situations where calls are charged and billed in two different locations. Furthermore, though the Alaska and Wisconsin courts had concluded that no carrier could assess any more than one state's tax on any one long distance call (under the local Bell Operating Company billing system that existed there then), GTE Sprint has submit-

ted uncontested evidence which demonstrates, that, by contrast, GTE Sprint could apply separate states' taxes on one interstate call bill. *See* Statement of the Case at 4. *Cf. Douglas*, 615 P.2d at 588; *Wisconsin Telephone*, 371 N.W.2d at 830. Thus, the Alaska and Wisconsin cases are no support whatsoever for the Illinois Supreme Court's analysis.[19]

Indeed, pertinent prior precedent points to a conclusion contrary to the one arrived at by the Illinois Supreme Court -- that the Illinois tax on long distance calls *originating* in Illinois can impose multiple tax burdens on the same activity. For example, in *Michigan-Wisconsin Pipe Line Co. v. Calvert*, 347 U.S. 157 (1954) ("*Michigan-Wisconsin*"), Texas had imposed a tax on the "taking" of gas into an interstate pipeline for interstate transmittal -- that is, on the "origination" of the interstate flow. The Court struck down the tax because, if Texas could place a tax on the origination of the interstate flow of gas, so, too, could the state where the interstate flow was terminated. *Michigan-Wisconsin*, 347 U.S. at 170. Likewise, here, if Illinois is permitted to apply a tax on the gross charge for an interstate call beginning in Illinois, so, too, must the state where the call terminates. Indeed, many states, such as Washington, New Mexico, and Ohio, have enacted taxes which permit them to tax calls terminating there, even if originating and charged to an address in Illinois. *See* App. A hereto. As a consequence, the Illinois tax is unconstitutional under proper case authority, and the Wisconsin

[19] In addition, the true underpinning of both the Alaska and Wisconsin courts' reasoning has simply been rejected by this Court. Both state courts had upheld the taxes at issue primarily because the plaintiffs had failed to demonstrate that the taxes at issue imposed *actual* multiple burdens. But, in *Armco Inc. v. Hardesty*, 467 U.S. 638 (1984), this Court categorically rejected this legal premise and held, instead, that actual multiple taxation need not be proven to invalidate a tax on interstate activity. The Wisconsin court also relied heavily on *General Motors Corp. v. Washington*, 377 U.S. 436 (1964) which has since been overturned or, at least, seriously eroded, in *Armco* and *Tyler Pipe Industries, Inc. v. Washington State Department of Revenue*, 107 S. Ct. 2810, 2817 (1987). *See* discussion *supra* at 32-33.

and Alaska state court decisions are inapposite to the issue here.

What is even more significant, however, is the fact that the Illinois Supreme Court simply conceded, after its extended analytical gyrations, that, with regard to long distance calls that end in Illinois, jurisdictions other than Illinois currently *do* tax those same calls.[20] The Illinois tax is patently void, then, by the Illinois Supreme Court's admission, because the imposition of the tax results in multiple taxation of interstate calls. *Armco Inc v. Hardesty*, 467 U.S. 638, 644-45 & n.8 (1984).

2. The Tax Discriminates despite the Credit Provision

The Illinois Supreme Court nevertheless managed to uphold the Illinois tax, by finding, with no discussion, that the credit provision in the Tax Act "cures" its admitted discriminatory effect. Under the Illinois credit provision, a taxpayer who has paid both Illinois' and another state's tax on the same call can receive a tax credit from Illinois in the amount of the other state's tax, but only if the taxpayer can prove (a) that a tax has already been paid on the same activity taxed by Illinois and (b) that the tax paid in the other state or states was "properly due." Examination of the actual operation of this credit mechanism reveals that it is no more than a snake-oil cure for multiple taxation, however, for discrimination persists, despite its operation.

To illustrate: If State X imposes a tax on the gross charge for a call made from State X to Illinois, at a rate of three percent, while Illinois imposes a tax on the gross charge for the same call as received in Illinois, at a rate of five percent, the fact that Illinois grants a credit to the taxpayer in the amount of three percent of the charge does not negate the fact that the charge for the call is still being taxed by State X *and* by Illinois, though the Illinois tax rate has now been effectively reduced to two percent.

[20] Here, the court was absolutely on target. For example, under the Oklahoma tax cited above, calls terminating in and charged to an Illinois service address could be taxed by Oklahoma, if the calls originate in Oklahoma and are billed there. *See* App. A hereto.

Further, the reduction of the Illinois tax rate is constitutionally meaningless because the division of tax between State X and Illinois, which is thus accomplished by the Illinois credit mechanism, will be completely arbitrary, based not on the percentage of substantive interstate call activity that goes on in each state, but on the relative absolute amounts of the two states' respective taxes. Thus, in the above example, Illinois would effectively receive tax on two-fifths of the call and State X on three-fifths -- regardless of what percentage of the taxed interstate calling activity occurred in either state. Such an arbitrary adjustment simply produces two non-apportioned taxes out of one and effectively multiplies discrimination.

Indeed, following the example, it is only when State X *happens* to assess a tax in an amount which equals or exceeds the absolute amount of the Illinois tax that the Illinois credit actually eliminates discrimination, by eradicating the Illinois tax altogether. This "cure" is totally fortuitous, however, and does not systematically purge the Illinois tax of its discriminatory disease, because it depends entirely upon the random and relative amounts of conflicting states' tax rates. *Halliburton Oil Well Cementing Co. v. Reily*, 373 U.S. 64, 76 (1963) (Brennan, J., concurring) (operation of credit based on amount of other state's tax provides only "fortuitous" and inadequate elimination of Commerce Clause infirmities).[21] The credit therefore fails to rescue the tax under the Commerce Clause.

Further, even if the Illinois credit mechanism did provide a reliable process for eliminating discrimination, the efforts it requires of taxpayers to participate in this process are enormous. For example, the Illinois tax credit is provided only for taxpayers

[21] Furthermore, to validate such a credit mechanism would only encourage states' legislatures to pass the highest politically possible tax on long distance calling they could. That is, by setting a higher tax than its neighbor, a state might retain tax revenues for itself, after credit offsets. However, it is this type of inexorable hydraulic pressure on interstate taxing that this Court rejected in *American Trucking Associations, Inc. v. Scheiner*, 107 S. Ct. 2829, 2842 (1987).

who can prove they have already paid to another state a tax which is "properly due," and which covers the same activity covered by the Illinois tax. *See* Statement of the Case, *supra* at 5. But no clarification of what taxes are deemed 'properly due' or overlapping in their application is provided by the taxing statute. Given this vagueness and the fact that long distance calling is a quotidian event, such a procedure will place an enormous burden of proof on interstate callers, not borne by callers calling instate. *See* Goldberg J.S. at 25-26. This burden is a burden on interstate commerce, in itself.

The State nevertheless defended the credit provision below, arguing that the adoption by numerous states of allegedly similar credit provisions in their use and sales tax schemes proves the Illinois credit effectively eradicates discrimination. The adoption of credit provisions in sales/use tax schemes in no way proves the Illinois credit mechanism is constitutional, however. First, the use/sales tax scheme has been devised to ensure that a state can tax the "use" of tangible goods within its boundaries when the sale of such goods takes place outside its borders, and the sale has not or cannot be taxed by another state. *See generally, Henneford v. Silas Mason Co.*, 300 U.S. 577 (1937). However, this Court has never determined whether sales and use taxes apply to overlapping or identical activity nor whether a credit provision in a use tax, for a paid sales tax, would be necessary to cure multiple taxation created by the imposition of both taxes. *Williams v. Vermont*, 472 U.S. 14, 22 (1985); *Henneford*, 300 U.S. 577, 587 (1937). Thus, it is not altogether clear whether the use/sales tax scheme even represents an example of multiple taxation -- or whether the credit provision in any particular use/sales tax scheme serves to alleviate unconstitutional discrimination.

Second, the typical sales and use tax situation appears to present dynamics which render the operation of the credit provision in the Illinois tax significantly more burdensome to the taxpayer than its operation would be to a taxpayer subject to a use tax. For example, it is a well-known fact that states have a difficult time collecting use taxes from consumers, due to jurisdic-

tional problems they encounter in enforcing collection by out-of-state sellers. Advisory Commission on Intergovernmental Relations, Pub. No. A-105, *State and Local Taxation of Out-of-State Mail Order Sales* (April, 1986); P. Hartman, *Collection of the Use Tax on Out-of-State Mail Order Sales*, 39 Vanderbilt L. Rev. 993, 1003-1004 (1986). *Cf. National Bellas Hess, Inc. v. Department of Revenue*, 386 U.S. 753 (1967). Thus, if the use tax is rarely collected from consumers because of jurisdictional problems, then the vast majority of consumers liable under use taxes will not encounter actual multiple taxation problems with great frequency -- nor find the need to resort to the credit provision.

The Illinois tax operates in a radically different manner. The tax requires long distance message carriers to tax *all* calls and it is unlikely that interstate carriers whose business spans the United States will be able to refuse collection on the ground that a state does not possess jurisdiction over it.[22] No long distance caller covered by the Illinois tax, or any like tax, will escape taxation. The burden will thus fall entirely on the credit provision to correct multiple burden problems. Given the proliferation and frequency of interstate calls, this burden will be immense -- and the taxpayer who makes long distance calls will bear it all, for each and every call.[23] For the State to maintain, then, that the use tax credit provisions demonstrate the validity of the Illinois credit provision is folly. Under the Illinois tax, those who engage in long distance phone calling and attempt to utilize the credit will bear huge burdens of recovery not borne by instate callers. The credit provision in the Tax Act therefore does not eradicate and, indeed, exacerbates the discriminatory effects of the tax.

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[22] Indeed, the tax virtually assures the carriers will impose the tax by making them equally liable for it. *See* Statement of the Case at 9.

[23] *See* Goldberg J.S. at 25-27 and authorities cited therein. Further, unlike the use/sales tax situation where there are normally only two taxing states involved in any one tax credit situation, the activity at issue here could easily involve the taxes -- and credit provision interactions -- of numerous states.

3. The Tax Discriminates by Imposing Heavier Burdens on Interstate than on Intrastate Calls

The State of Illinois argued below that the Illinois tax could not be deemed "discriminatory" because the same or "equal" five percent tax was levied on both interstate and intrastate calls in Illinois. The gist of the argument is that the five percent tax on interstate calls is a "compensating" tax, *i.e.*, a tax that equalizes the tax burdens on intra- and interstate activities. *Cf. Henneford v. Silas Mason Co.*, 300 U.S. 577 (1937). The Illinois Supreme Court apparently agreed. Goldberg J.S. App. C at 11a. However, the Illinois tax on interstate calls cannot be justified as a tax which is either "equal" to the five percent tax on intrastate calls, nor one which "compensates" for it.

First, it does not follow that simply because a flat five percent tax is applied to both intra- and interstate calls, the tax does not discriminate against interstate commerce. Just last term, this Court struck down such a facially "equal" tax, stating: "[T]he Commerce Clause has a deeper meaning that may be implicated even though state provisions ... do not allocate tax burdens between insiders and outsiders in a manner that is facially discriminatory." *American Trucking*, 107 S. Ct. at 2839. In *American Trucking*, an equal and flat tax was applied to trucks in both intra- and interstate commerce, for the privilege of utilizing Pennsylvania's highways. Despite this "equality" of taxing, the Court held that the interstate carriers were bearing a proportionately heavier tax burden than the instate carriers, because interstate carriers did not use instate facilities with nearly the frequency instate carriers did:

> Although out-of-state carriers obtain a privilege to use Pennyslvania's highways that is nominally equivalent to that which local carriers receive, imposition of the flat taxes for a privilege that is several times more valuable to a local business than to its out-of-state competitors is unquestionably discriminatory and thus offends the Commerce Clause.

American Trucking, 107 S. Ct. at 2847. Similarly, the allegedly

"equal" Illinois tax is proportionately higher on interstate than on intrastate calls, because interstate calls do not utilize instate facilities for calls as extensively as instate calls do, as GTE Sprint has demonstrated by uncontested fact. *See* Statement of the Case at 3-4. The interstate tax is therefore not "equal" to the instate tax. *American Trucking*, 107 S. Ct. at 2846.

Second, the tax on interstate calls does not merely "compensate" for the imposition of the five percent tax on instate calls, under the "compensating tax" doctrine. As this Court has stated, "[t]he concept of a compensatory tax first requires identification of the burden for which the state is attempting to compensate." *Maryland v. Louisiana*, 451 U.S. 725, 758 (1981). Here, the only burden for which the Illinois tax is arguably compensating is the burden of supporting calling or transmission activity. But the burden on Illinois of supporting interstate calling is nowhere near its burden of supporting instate calls because *all* the activity involved in instate calling will occur in Illinois, whereas only part of it will with regard to interstate calls. Thus, the two different events -- instate and interstate calling -- do not impose comparable burdens on the State, and are not, under the compensating tax doctrine, "substantially equivalent event[s]." *Armco*, 467 U.S. at 643. The flat five percent tax on both intra- and interstate calling in the Tax Act does not fall equally on the two. Instead, it overcompensates Illinois for the burdens interstate transmission places on the state, because Illinois' burden is lighter with regard to such transmission. The result is that "[r]ather than 'compensating' [Illinois] for a supposed . . . disadvantage . . . the [Illinois tax] . . . creates . . . both an advantage for [Illinois instate callers] . . . and a discriminating burden on commerce to its sister States." *Boston Stock Exchange v. State Tax Commission*, 429 U.S. 318, 331 (1977). *See also Tyler Pipe*, 107 S. Ct. 2810, 2818 (1987). Since "[t]he common thread through the cases upholding compensatory taxes is the equality of treatment between local and interstate commerce," it is clear the Illinois five percent/five percent tax scheme cannot be justified under the "compensatory tax" doctrine. *Maryland v. Louisiana*, 451 U.S. at 759; *American Trucking*, 107 S. Ct. at 2846.[24]

C. The Tax Violates the Commerce Clause because It Is Not Fairly Related to Services Provided by Illinois

A state tax on interstate activity must be "fairly related to the services provided by the State." *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977). GTE Sprint argued below that the Illinois tax failed this fourth *Complete Auto* test. The Illinois Supreme Court disagreed, concluding that "the services provided by [Illinois] facilitate perhaps the most critical step in the taxable event -- interstate origination . . . [while] . . . the benefits afforded by other States in facilitating the same interstate telecommunication are too speculative to override the substantial benefits extended by Illinois." Goldberg J. S. App. C at 13a (emphasis added). This assumption has no basis in fact, however, as uncontroverted evidence submitted below establishes the highly significant role of states other than Illinois in facilitating interstate telecommunications, even where they begin in Illinois. *See* Statement of the Case at 3-4; Sprint J.S. App. C at 7a-8a.

There is also no legal basis for concluding that the Illinois tax has any fair relation to the services Illinois provides the taxed activity. The fair relation test requires that:

> [t]he *measure* of the tax must be reasonably related to the extent of the [activity's] contact [with the taxing

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[24] In this respect, the Illinois intra- and interstate tax scheme is totally different from a use/sales tax "compensatory" scheme which applies to tangible personal property that is sold entirely in one state and is then entirely consumed within another. *Cf. Henneford v. Silas Mason Co.*, 300 U.S. 577 (1937). Interstate service simply does not represent a distinguishable and totally out-of-state counterpart to some totally instate activity, as the "use" of a product outside a state may be the counterpart to the sale of it within another. Therefore, although the sales/tax scheme may provide that "the stranger from afar is subject to no greater burdens . . . than the dweller within the gates," this is certainly not the case here. *Henneford*, 300 U.S. at 584.

> state], since it is the activities or presence of the taxpayer in the State that may properly be made to bear a 'just share of the state tax burden. [T]he incidence of the tax *as well as its measure* [must be] tied to the earnings which the State . . . has made possible. . . .'

Commonwealth Edison Co. v. Montana, 453 U.S. 609, 626 (1981) (emphasis in text) (citations omitted). But the measure of the Illinois tax is not tied to the earnings or charges which Illinois has made possible with regard to interstate calling. As GTE Sprint proved by uncontested affidavit, interstate calling involves significant transmission activities outside Illinois, which activities are economically supported by other states. *See* Statement of the Case at 3-4 . The Illinois tax applies to the full stretch of every interstate call, however, though the activity taxed has only partial presence in, and is only partially supported by, Illinois.

In this respect, the infirmity of the Illinois tax strongly resembles the flaw of the flat privilege tax on interstate carriers, struck down in *American Trucking Associations, Inc. v. Scheiner*, 107 S. Ct. 2829 (1987). There, the Court stated that:

> A tax levied for the privilege of using roads, and not their actual use, may, in the normal course of operations, and not as a fanciful hypothesis, involve an undue burden on interstate carriers. While the privilege extended by a State is . . . theoretically the same for all vehicles, whether interstate or intrastate, the intrastate vehicle can and will exercise the privilege whenever it is in operation, while the interstate vehicle must necessarily forego the privilege some of the time simply because of its interstate character, *i.e.*, because it operates in other states as well. In the general average of instances, the privilege is not as valuable to the interstate as to the intrastate carrier.

American Trucking, 107 S. Ct. at 2844 (citations omitted). Likewise, here, the privilege Illinois accords interstate callers is worth significantly less than that afforded instate callers because instate callers use Illinois facilities and lines more frequently. The Illinois tax, which taxes both equally, therefore "bears no relationship to the taxpayers' presence or activities in [the]

State. . . ." *American Trucking*, 107 S. Ct. at 2844; *Nippert v. Richmond*, 327 U.S. 416 (1946) (flat tax on solicitors whether operating intra- or interstate bore no relation to volume of instate business done or returns from it).

Indeed, the Illinois tax is even less 'fairly related' and is, therefore, more insidious than the tax the Court invalidated in *American Trucking*, because the Illinois tax tends to tax a call *more* heavily, the *less* the call involves instate activity. As the uncontested facts show, calls made over greater distances tend to cost more and GTE Sprint (therefore) tends to charge more for such calls. The further tendency is that, the greater the distance of a call touching Illinois, the more out-of-state or non-Illinois activity it involves. *See* Statement of the Case at 3-4 . But, because Illinois receives a flat five percent on the gross charge for calls, Illinois tends to receive more revenue on calls the longer -- and more expensive -- they are and, therefore, the more they involve activity outside the State of Illinois. *See* Sprint J. S. App. C at 8a-9a. The tax therefore operates in direct contradiction to the dictates of the fair relation rule because there is an inverse relationship between the amount of Illinois activity involved in a long distance call and the measure of the Illinois tax. This insidious inverse relationship assures that the Illinois tax is out of all proportion to the extent of the taxpayers' activities in Illinois -- and that it is unconstitutional under established Commerce Clause principles. *See American Trucking*, 107 S. Ct. 2829, 2844 (1987); *Commonwealth Edison Co. v. Montana*, 453 U.S. 609, 627-29 (1981).

CONCLUSION

The judgment of the Illinois Supreme Court that the Illinois Tax Act is constitutional under the Commerce Clause was in error. The court's judgment should therefore be reversed.

Respectfully submitted,

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APPENDICES

APPENDIX A

SUMMARY OF SELECTED EXISTING TAXES ON INTERSTATE TELECOMMUNICATIONS ACTIVITY

Arkansas Gross Receipts Act of 1941, Ark. Stat. Ann. § 26-52-301 (Supp. 1987), effective February 11, 1987 (taxing interstate long distance messages which originate or terminate in Arkansas and are billed to an Arkansas telephone number or customer location).

Colorado Emergency Retail Sales Tax Act of 1935, Colo. Rev. Stat. § 39-26-104(1)(c) (1982), interpreted in Revenue Bulletin 83-7, October 1983 (imposes tax on interstate access charges).

Florida Revenue Act of 1949, Fla. Stat. Ann. § 212.05 (1)(e)2 (West Supp. 1988), effective July 1, 1986 (taxing telecommunications services which originate or terminate in Florida and are billed to a customer, telephone number, or device in Florida and, with regard to interstate private line communication services, taxing only that percentage of the service charge corresponding to the percentage of total call mileage within the state).

Greeley, Colorado City Ordinance No. 45, effective July 1, 1985 (taxing interstate telecommunications services originating from or received on telecommunication equipment in Greeley if the charge for the service is billed or charged to an apparatus, telephone, or account in Greeley, or to a customer location in Greeley, or to a person residing in Greeley).

Los Angeles, California Ordinance No. 162586, effective July 7, 1987 (taxing every person using and paying for interstate telephone exchange services in the City of Los Angeles).

Minnesota Tax Reform and Relief Act of 1967, Minn. Stat. Ann. § 297A.01. subd. 3(f) (West Supp. 1988), effective June 1, 1987 (taxing interstate toll service originating in Minnesota and charged to a telephone located in Minnesota).

New Mexico Gross Receipts and Compensating Tax Act, N.M. Stat. Ann. §§ 7-9-3(F); 7-9-4; 7-9-56 (1986 Repl.), effective July 1, 1988 (taxing interstate and international messages or conversations that originate or terminate in New Mexico and are billed to a New Mexico telephone number or account).

Ohio Sales Tax Act, Ohio Rev. Code Ann. § 5739.01 (B)(3)(f) (1987 Supp., p. 67), effective October 20, 1987 (taxing telecommunications service originating or terminating in Ohio and charged to the consumer's telephone number or account in Ohio).

Oklahoma Sales and Use Tax, Okla. Stat. Ann. tit. 68, § 1354(D) (West Supp. 1988), interpreted by Oklahoma Tax Commission Order No. 83-01-10-06, effective January 10, 1983 (taxing sale of all long distance calls which originate in Oklahoma and where calls are billed to Oklahoma subscribers or users).

Texas Limited Sales, Excise, and Use Tax Act, Tex. Tax Code Ann. § 151.323(1) (Vernon Supp. 1988), effective November 1, 1987 (taxing receipts from the sale, use or consumption in Texas of long-distance telecommunications services that are originated from and billed to a telephone number or billing or service address within Texas).

Washington Revenue Act of 1935, Wash. Rev. Code Ann. § 82.04.065(2) (Supp. 1988), effective July 1, 1983 (taxing interstate telecommunications service originating or terminating in Washington and billed to a person in Washington).

Wheat Ridge, Colorado Ordinance No. 630, effective August 27, 1985 (taxing interstate telecommunications services charged to an apparatus, telephone, or account in Wheat Ridge, or to a customer location within Wheat Ridge, or to a person residing in Wheat Ridge).

Wisconsin General Retail Sales Tax Act, Wis. Stat. Ann. § 77.52(2)(a)(4) (West Supp. 1987), effective May 1, 1982 (taxing interstate service originating in Wisconsin and charged to a telephone located in Wisconsin).

Wisconsin General Retail Sales Tax Act, Wis. Stat. Ann. § 77.51(14)(m) (West Supp. 1987) (sales tax imposed upon transfers of services permitting the origination and termination of telephone messages).

APPENDIX B

BEFORE THE OKLAHOMA TAX COMMISSION

STATE OF OKLAHOMA

IN THE MATTER OF THE AMENDMENT TO ORDER NO.'S 82-12-21-01 AND 82-12-13-03 REGARDING THE APPLICATION OF THE SALES TAX IN THE SALE OF LONG DISTANCE TELEPHONE SERVICE.	Ref. 82-12-21-01 82-12-13-03

ORDER NO. 83-01-10-06

This matter comes on before the Oklahoma Tax Commission upon the various Motions to vacate, stay and reconsider the captioned Orders and upon the request of the Sales and Use Tax Division and the Legal Division for an Order vacating Orders Numbered 82-12-21-01 and 82-12-13-03 and for a new order applicable to the various telephone companies, operating within the State of Oklahoma, concerning the application of the Oklahoma sales tax on the sale of long distance telephone service. The Commission proceeded to review the files and records in this matter, hear recommendations of the Sales and Use Tax Division and advice of legal counsel, and the arguments of various telephone companies which were represented by Bill Anderson, William Free and Ron Comingdeer, being considered and being fully advised in the premises, finds:

(1) Title 68 O.S. 1981, Section 1354, Subsection (D) imposes Oklahoma sales tax upon the sale of service provided by a telephone company including local and long distance service as follows:

Title 68 O.S. 1981, Section 1354:

"There is hereby levied upon all sales, not otherwise exempted in this article, an excise tax of 2% of the gross receipts or gross proceeds of each sale of the following:

(D) Service by telephone or telegraph companies to subscribers or users, including transmission of messages, whether local or long distance and all services and rental charges in connection with transmission of any message; . . . "

(2) "Telephone company", for purposes of this Order, means any person, firm, association, partnership, corporation or other legal entity who offer for sale within this state any telephone transmission service.

(3) "Originated within this state", for purposes of this Order, means any Long Distance Message Telecommunication Services ("long distance telephone service or calls" herein) which are sold to an Oklahoma subscriber or user within this state, including calls initiated in Oklahoma and terminated within or without Oklahoma and billed to the Oklahoma subscriber or user and calls initiated without Oklahoma and billed collect to a subscriber or user within Oklahoma.

(4) Although 68 O.S. 1981, Section 1354 provides for an excise tax of 2% of the gross receipts of the sale of service by telephone companies to subscribers or users, including transmission of messages, whether local or long distance, it appears from the files and records that said telephone companies collect, report and remit the excise tax only on all long distance telephone service, if the calls originate within this state and terminate within this state. But, some said telephone companies have failed, neglected or refused to collect, report and remit the excise tax on any and all long distance telephone services, if the calls originate within this state and terminate outside this state.

(5) The Oklahoma Sales Tax Code does not exempt said telephone companies from collecting, reporting, remitting or paying excise tax on the sale, within this state, of long distance telephone services billed to Oklahoma subscribers or users whether such long distance calls terminate or originate within or without this state.

(6) Certain telephone companies operating within the State of Oklahoma do not declare total gross receipts, both taxable and nontaxable, on Line 1 of the sales tax report, as required in §1365(A), nor do they identify all legal deductions on Lines 4A through 4G. The failure to report such information hinders an office audit determination of the proper amount of sales tax being reported, collected, remitted or paid. And this Commission is empowered and authorized to require sales tax reporters to furnish information necessary to compute the state sales tax by 68 O.S. 1981, §206, 243 and 1365.

Title 68 O.S. 1981, Section 1365, states in part:

> "(A) The tax levied hereunder shall be due and payable on the first day of each month, except as herein provided, by any person liable to remit or pay any tax due under this acticle. For the purpose of ascertaining the amount of the tax payable under this article, it shall be the duty of all tax remitters, on or before the 15th day of each month, to deliver to the Tax Commission, upon forms prescribed and furnished by it, sales tax reports signed under oath, showing the gross receipts or gross proceeds arising from all sales taxable or nontaxable under this article during the preceding calendar month. Such reports shall show such further information as the Tax Commission may require to enable it to compute correctly and collect the tax herein levied . . . "

(7) The Sales and Use Tax Division is currently reviewing the administration and enforcement of Subsection D of §1354 as to applicability of Oklahoma sales tax upon all sales of all types of various services by telephone companies in Oklahoma; and, the Division is currently engaged in field audits of one or more of said telephone companies regarding all such telephone services sold within this State.

(8) This Order should not in any way or manner be construed to limit, restrict or negate the current efforts of the Sales and Use Tax Division, but rather, this Order should be limited to and only applicable to the administration and enforcement of sales tax on the sale of long distance telephone services to Oklahoma subscribers or users.

(9) Order No.'s 82-12-21-01 and 82-12-13-03 should be vacated and all telephone companies shall be bound by the findings herein set forth.

NOW, THEREFORE, IT IS HEREBY ORDERED by the Oklahoma Tax Commission, effective with the date of this Order, that Orders numbered 82-12-13-03 and 82-12-21-01 be, and hereby are, vacated and of no force and effect.

IT IS FURTHER ORDERED by the Oklahoma Tax Commission, that all telephone companies doing business within the State of Oklahoma are ordered to collect, report, remit, or pay to the Sales and Use Tax Division of the Oklahoma Tax Commission the 2% sales tax levied in 68 O.S. 1981, Section 1354 and imposed upon the sale of all long distance telephone services originated within this State and billed to Oklahoma subscribers or users, without regard to whether the billed, long distance telephone calls terminate within or without this state.

IT IS FURTHER ORDERED by the Commission that each and every telephone company doing business within the State of Oklahoma, with 68 O.S. 1981, Section 1365(A), in its monthly sales tax report Form 13-15, shall properly identify total gross receipts, both taxable and nontaxable, and appropriate statutory deductions, all as set out in the Commission approved Form 13-15.

IT IS FURTHER ORDERED that the Sales and Use Tax Division shall notify the telephone companies operating within this State that Oklahoma state sales tax and any applicable municipal sales tax will immediately be collected, reported, and remitted or paid on all long distance telephone services originated within this State and billed to Oklahoma subscribers or users on all bills dated no later than February 15, 1983 and all subsequent billings for such services to Oklahoma subscribers or users.

DATED this JAN 10 1983.

OKLAHOMA TAX COMMISSION

SEAL

ATTEST:

/s/ MARY JANE SINCLAIR	/s/ ODIE A. NANCE
Assistant Secretary	Odie A. Nance Chairman
APPROVED:	
/s/ HAROLD W. DOZIER	/s/ ROBERT L. WADLEY
Harold W. Dozier, Director Sales and Use Tax Division	Robert L. Wadley, Vice-Chairman
APPROVED AS TO FORM:	
/s/ J. LAWRENCE BLANKENSHIP	/s/ J. L. MERRILL
J. Lawrence Blankenship General Counsel	J. L. Merrill, Secretary-Member
/s/ DONNA E. COX	
Donna E. Cox, Attorney	

APPENDIX C

[COLORADO]

REVENUE BULLETIN
83-7
OCTOBER - 1983

Issue: Are "carrier access charges" and "customer access line charges" (i.e. telephone service rate charges to interexchange carriers and local telephone subscribers) subject to Colorado sales tax?

Dept. Position: Both "carrier access charges" and "customer access line charges" are subject to Colorado sales tax pursuant to the provisions of C.R.S. 39-26-104(1)(c). Under this section, a Colorado sales tax is to be levied upon all intrastate telephone service. It is the Department's position that the services being provided for which "carrier access charges" and "customer access line charges" are assessed constitute "intrastate telephone service" and are therefore taxable.

APPENDIX D

[LOS ANGELES, CALIFORNIA]

ORDINANCE NO. 162586

An ordinance amending the Telephone Users Tax to include charges for interstate and international calls in the measure of tax.

THE PEOPLE OF THE CITY OF LOS ANGELES DO ORDAIN AS FOLLOWS:

Section 1. Subsection (a) of Section 21.1.3 of the Los Angeles Municipal Code is hereby amended to read as follows:

(a) There is hereby imposed a tax upon every person in the City of Los Angeles using telephone communication services including services for intrastate, interstate, or international calls, and using any teletypewriter exchange services in the City of Los Angeles. The tax imposed by this section shall be at the rate of 5 percent of the charges made for such services and shall be paid by the person paying for such services. Interstate calls shall be deemed to include calls to the District of Columbia.

Sec. 2. The first sentence of subsection (c) of Section 21.1.3 of the Los Angeles Municipal Code is hereby amended to read as follows:

The tax imposed in this section shall be collected from the service user by the person providing the telephone communication services or the teletypewriter exchange services.

Sec. 3. Subsection (d) of Section 21.1.3 of the Los Angeles Municipal Code is hereby amended to read as follows:

(d) Notwithstanding the provisions of Subsection (a), the tax imposed under this section shall not be imposed upon any person for using telephone communications services or teletypewriter exchange services, to the extent that the amounts paid for such services are exempt from or not subject to the tax imposed under Sec. 4251 of Title 26 of the United States Code, as such Section existed on November 1, 1967.

Sec. 4. Section 21.1.8 of the Los Angeles Municipal Code is amended by adding subsection (c) thereto to read as follows:

(c) The duty to collect the tax based on a measure including charges for interstate and international communication services or interstate and international teletypewriter exchange services shall commence with the first regular billing period of each service user ending on or after October 1, 1987.

Sec. 5. Any portion of Section 21.1.3(a), or of the first sentence of Section 21.1.3(c), or any portion of Section 21.1.3(d), or of Section 21.1.8(c) of the Los Angeles Municipal Code as amended by either Ordinance No. 162, 422 or Ordinance No. 162, 522 or both, and inconsistent with this ordinance shall have no force or effect after June 28, 1987.

Sec. 6. The City Clerk shall certify to the passage of this ordinance and cause the same to be published in some daily newspaper printed and published in the City of Los Angeles.

I hereby certify that the foregoing ordinance was introduced at the meeting of the Council of the City of Los Angeles of June 30, 1987 and was passed at its meeting of July 7, 1987.

Approved **July 7, 1987** ELIAS MARTINEZ, City Clerk

By: /s/ KYLE TAYLOR
deputy

File No. **87-0838-51** /s/ TOM BRADLEY
Mayor

APPENDIX E

[AMENDMENT TO ORDINANCE NO. 630
OF THE CITY OF WHEAT RIDGE, COLORADO]

[*See* GTE Sprint J.S. App. E at 14a-15a]

Telecommunications Service: "Telecommunications Service" means the transport of signs, signals, writing, images, sounds, messages, data, or other information of any nature by wire, radio, light waves, electromagnetic, digital, or electronic means, except carrier access services or interstate private communication services as defined herein.

Private Communication Service: "Private Communication Service" means:

(1) The communication service furnished to a subscriber which entitles the subscriber:

(A) to exclusive or priority use of any communication channel or groups of channels, or

(B) to the use of an intercommunication system for the subscriber's stations,

regardless of whether such channel, groups of channels, or intercommunication system may be connected through switching as herein described,

(2) Switching capacity, extension lines and stations, or other associated services which are provided in connection with, and are necessary or unique to the use of, channels or systems described in paragraph (1), and

(3) The channel mileage which connects a telephone station located outside a local telephone system area with a central office in such local telephone system,

except that such term does not include any communication service unless a separate charge is made for such service. . . .

(b) There shall be levied a tax upon the sale of telecommunications services, whether furnished by public or private corporations or enterprises for all intrastate, interstate and international telecommunications service charged to an apparatus, telephone, or account in Wheat Ridge, or to a customer location within Wheat Ridge, or to a person residing in Wheat Ridge, without regard to where the bill for such service is physically received. For purposes of this section, "telecommunications service" includes the installation of any telecommunications equipment or apparatus. A credit shall be allowed to the extent provided in Section 21-11(d) for any telecommunications services subject to the tax herein that are also subject to a sales tax outside of this City. . . .

(11) "Carrier Access Services" by local telephone exchange companies to providers of telecommunication service for use in providing such service shall be deemed to be wholesale sales and shall be exempt from taxation under this section.

APPENDIX F

[GREELEY, COLORADO MUNICIPAL CODE TITLE 4 CITY RETAIL SALES AND USE TAX ORDINANCE]

4.04.005 Short title. This chapter, together with Chapters 4.08 and 6.08, may be known and cited as the "City Retail Sales and Use Tax Ordinance". . . .

4.04.015 Definitions. A. "Access services" means any charge by local telephone exchange companies to providers of telecommunications services for use in providing their telecommunications services. . . .

U. "Telecommunications services" means the transport of signs, signals, writings, pictures, images, sounds, messages, data, or other information of any nature by wire, radio, light waves, electromagnetic, digital, or electronic means, except carrier access services or interstate private communication services. . . .

4.04.060 Sales tax--Levied. There is levied and there shall be collected and paid a sales tax in the amount stated in Section 4.04.145 as follows. . . .

E. Upon telecommunications services, except carrier access services and interstate private communication services as designated in Section 4.04.015U, whether furnished by public or private corporations or enterprises for all interstate, intrastate, and international telecommunications services originating from or received on telecommunications equipment in Greeley if the charge for the service is billed or charged to an apparatus, telephone, or account in Greeley, or to a customer location in Greeley, or to a person residing in Greeley, without regard to where the bill for such service is physically received. . . .

4.04.065 Sales tax--Imposed on full purchase price. The sales tax is imposed on the full purchase price of articles sold after manufacture or after having been made to order and includes the full purchase price of materials used and service performed

in connection therewith, excluding, however, such articles as are otherwise exempted. . . .

4.04.142 Sales tax--Credit for sales or use taxes previously paid to another municipality. For transactions consumated [sic] on or after January 1, 1986, the city's sales tax shall not apply to the sale of tangible personal property at retail or the furnishing of services if the transaction was previously subject to a sales or use tax lawfully imposed on the purchaser or user by another statutory or home rule municipality equal to or in excess of three percent. A credit shall be granted against the city's sales tax with respect to such transaction equal in amount to the lawfully imposed local sales or use tax previously paid by the purchaser or user to the previous statutory or home rule municipality. The amount of the credit shall not exceed three percent. . . .

4.04.145 Sales tax--Amount designated. There is imposed, upon all sales of commodities and services specified in Section 4.04.060, a sales tax in accordance with the following schedule:

Amount of Sale	Sales Tax
$0.00 to and including $0.17	No tax
0.18 to and including 0.49	$0.01
0.50 to and including 0.83	0.02
0.84 to and including 1.00	0.03

On sales in excess of one dollar, the tax shall be three cents on each full dollar of taxable sales, plus the tax shown in the above schedule for the applicable fractional part of a dollar of each such sale price. . . .

4.04.150 Sales tax--Retailers and vendors to add tax to price or charges--Status of tax as debt--Nonresident retailers and vendors--Tax collection. Retailers and vendors shall add the tax imposed hereby, or the average equivalent thereof, to the sale price or charge, showing such tax as a separate and distinct item, and when added, such tax shall constitute a part of such price or charge and shall be a debt from the consumer or user

to the retailer until paid, and shall be recoverable by law in the same manner as other debts. Nonresident retailers and vendors engaged in business in the city shall collect and remit the sales tax as prescribed in this section. . . .

Nos. 87-826, 87-1101

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

JEROME F. GOLDBERG and ROBERT McTIGUE,
Appellants,

v.

ROGER D. SWEET, DIRECTOR OF THE ILLINOIS DEPARTMENT OF REVENUE, et al.,
Appellees.

GTE SPRINT COMMUNICATIONS CORPORATION,
Appellant,

v.

ROGER D. SWEET, DIRECTOR OF THE ILLINOIS DEPARTMENT OF REVENUE, et al.,
Appellees.

On Appeal From The Supreme Court Of Illinois

CONSOLIDATED BRIEF OF APPELLEES

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QUESTION PRESENTED

Does the Illinois Telecommunications Excise Tax Act, which imposes a 5% tax on all intrastate telecommunications and on only those interstate telecommunications which are originated in or received in Illinois *and* charged to an Illinois service address, satisfy contemporary Commerce Clause requirements which mandate that a tax not discriminate on the basis of state lines, be fairly apportioned and bear a fair relation to the activity of the taxpayer in the taxing state?

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On Appeal From The Supreme Court Of Illinois

CONSOLIDATED BRIEF OF APPELLEES

STATEMENT OF THE CASE

Appellants Jerome Goldberg and Robert McTigue filed suit in the Circuit Court of Cook County, Illinois, alleging that Section 4 of the Illinois Telecommunications Ex-

cise Tax Act, Ill. Rev. Stat. ch. 120, paras. 2001-2021 (1987) (the "Act"), (Goldberg Jurisdictional Statement Appendix ("Goldberg J.A.") at 25a) violated the Commerce Clause of the Constitution of the United States. U.S. Const. art. I, §8, cl. 3. Appellant GTE Sprint Communications Corporation ("GTE"), a defendant in the Circuit Court suit, filed a cross-claim against the State of Illinois based on the same alleged constitutional infirmity.[1] Section 4 of the Act provides that:

> A tax is imposed upon the act or privilege of originating in this State or receiving in this State interstate telecommunications by a person in this State at the rate of 5% of the gross charge for such telecommunications purchased at retail from a retailer by such person. To prevent actual multi-state taxation of the act or privilege that is subject to taxation under this paragraph, any taxpayer, upon proof that the taxpayer has paid a tax in another state on such event, shall be allowed a credit against the tax imposed in this Section to the extent of the amount of such tax properly due and paid in such other state.

Ill. Rev. Stat. ch. 120, para. 2004 (1987). (Goldberg J.A. at 29a.)

On cross motions for summary judgment seeking a determination of the constitutionality of Section 4 of the Act, the Circuit Court of Cook County, Illinois, held that Section 4 violated the Commerce Clause of the United States Constitution. (Goldberg J. A. at 18a.)[2] The State of Illinois

[1] Appellants also raised due process and equal protection claims under the United States and Illinois Constitutions; these claims have been abandoned.

[2] The record before the trial court on the cross motions contains virtually no factual evidence. In the cross motions, the State of Illinois, appellants Goldberg and McTigue and appellant GTE dealt with the statute on its face. GTE submitted a short affidavit which

(Footnote continued on following page)

took a direct appeal to the Illinois Supreme Court, which reversed the Circuit Court. (Goldberg J. A. at 17a.) On July 27, 1987, the Illinois Supreme Court issued an opinion, *Goldberg v. Johnson*, 117 Ill. 2d 493, 512 N.E.2d 1262 (1987). (Goldberg J. A. at 4a.)

Sections 2(a) and 2(b) of the Act define "gross charge" (on which Section 4 of the Act bases the tax) as "the amount charged to the taxpayer's service address" in Illinois. Ill. Rev. Stat. ch. 120, para. 2002. (Goldberg J. A. at 25a-26a.) The typical station-to-station interstate telephone call *from* a person in Illinois—a call originated in Illinois and charged to a service address in Illinois—yields a "gross charge" equal to the cost of the call, and the call is taxed by Illinois. The typical station-to-station interstate telephone call *to* a person in Illinois—a call received in Illinois but charged to an originating service address outside Illinois—yields a "gross charge" of zero, and the call is not taxed by Illinois. Similarly, a collect call originated in Illinois but charged to a non-Illinois service address yields a gross charge of zero. In its practical application, the Act levies a tax on every telephone call to or from a person in Illinois that is also charged to an Illinois service address, but exempts from tax every interstate call that is not both originated or received in Illinois and charged to an Illinois service address.

In its opinion, the Illinois Supreme Court evaluated the Act according to its practical effect:

[2] *continued*

described certain aspects of GTE's business. (GTE Jurisdictional Statement Appendix ("GTE J.A.") at 7a-10a.) That affidavit is incomplete as to GTE and is silent as to the business of other interstate telephone companies. The Illinois Supreme Court's review was limited to an analysis of the statute on its face.

> The tax, by its terms, applies only to interstate telecommunications originating or received in Illinois and paid for in Illinois or billed to a service address in Illinois. Not only does the taxable event transpire in Illinois but the "gross charge" for the taxable event must be paid for in Illinois or billed to an address in Illinois.

(Goldberg J. A. at 10a.)

The Illinois Supreme Court reasoned that the Act satisfied the four prongs of the test enunicated by this Court in *Complete Auto Transit, Inc. v. Brady*, 439 U.S. 274, 279 (1977), and used to determine whether a state tax is constitutional under the Commerce Clause and stated that the tax nexus of Illinois over the persons and events taxed by the Act was undisputed; the Act satisfied the apportionment requirement because it did not produce a risk of multiple taxation; the Act did not discriminate against interstate commerce and its credit provision would mitigate any actual multiple taxation; and the measure of the tax under the Act was fairly related to the benefits provided by Illinois to the taxpayer.

SUMMARY OF ARGUMENT

The Illinois Telecommunications Excise Tax Act generates funds for the general revenue of the State of Illinois by imposing a 5% tax on intrastate and interstate telephone calls purchased at retail, when the telephone call is originated or received in Illinois and charged to an Illinois service address. The amount of the tax is a function of the charge for the telephone call and does not depend on whether the telephone call is interstate or within Illinois.

Appellants do not contend that any tax immunity arises solely from the fact that the subject of the challenged tax is an interstate telephone call. It is by now too well settled to require extended discussion that a state may tax interstate commerce, provided that the State possesses the requisite nexus to the taxed transaction and that the tax, as practically applied, does not discriminate against or unfairly burden interstate commerce. Thus, the question here is not whether Illinois may tax interstate telecommunications, but whether the tax Illinois designed is constitutional.

Appellants' Commerce Clause objections to the Act have a single focus—the fact that the tax is assessed on the entire cost of those interstate calls to which it applies. This results, in their view, in three related violations of the *Complete Auto* test for measuring the validity of a state tax under the Commerce Clause.

1. Appellants contend that the tax violates the "second prong" of the *Complete Auto* test, the requirement of fair apportionment. In effect, appellants seek to have this Court judicially legislate a tax different and considerably less practical than the Act. Appellants' central premise is that in any long distance call at least two states (those where the originator and the recipient to the call are located) have nexus to tax an interstate call. Further, appellants suggest that intervening states through which a call might pass have nexus and are also entitled to a share of the tax base. They then reason that Illinois may not tax more than its fair share (presumably, 50% or less) of any interstate call. By basing the tax on the entire cost of any taxed call, Illinois has, appellants insist, taken more than its fair share as its tax base.

Appellants' argument depends upon a purposeful distortion of the practical operation of the interstate telecom-

munication system and the governing law. The interstate telephone system is a complex electronic network that does not send each interstate call over a standard route. Moreover, appellants' argument ignores the fact that the tax is imposed only on those telephone calls that meet the statutory requirements of origination or receipt in Illinois and a charge to an Illinois service address. Illinois does not tax those numerous other interstate telephone calls which, although they originate in, are received in, or pass through Illinois, are not charged to an Illinois service address. Inasmuch as appellants' premise is that at least two states might tax a telephone call, their argument becomes a demand for apportionment of every call.

The Act fully and fairly apportions the universe of telephone transactions between Illinois and other states. Moreover, the Act is no different in its practical effect and economic substance than sales, use and gross receipts taxes that have been approved by this Court.

Lastly, any possible deficiency in apportionment is guarded against by the credit mechanism of the Act, which provides that a taxpayer who has paid a tax to another jurisdiction on an interstate call charged to the taxpayer's Illinois address shall receive a credit against his liability under the Act. This provision serves to adequately apportion the tax in and of itself.

2. The appellants contend that in its practical effect, the Act treats interstate and intrastate commerce differently. The appellants' argument is without support. The Act, both on its face, and in practical application, treats interstate and intrastate commerce identically. This is confirmed by application of the "internal consistency" principle. If every state adopted the same tax as that imposed by Illinois, no call would be taxed on more than 100% of its cost. In order to avoid the conclusion that the Act

satisfies the principle of "internal consistency", the appellants seek to expand the concept of internal consistency by hypothesizing different tax systems in different states, and considering the cumulative effect of those different systems on carefully selected examples. There is no support for expanding the internal consistency test in this fashion.

The Act also satisfies what this Court has called the requirement of "external consistency"—that the basis chosen for determining the taxing state's share of the total tax potential not produce grossly distorted results. Appellants have made no showing that a disproportionate share of interstate calls are charged to the service address of the Illinois participant. Accordingly, the Act is externally consistent.

3. Finally, the Illinois tax is faulted on the ground that its measure—the cost of the call charged to a customer—lacks a fair relation to the protection or services provided by the State to that customer. Fair relation is violated, appellants claim, because distance is one of the main variables affecting the cost of a call and a large part of the distance between the parties to most interstate calls will be outside Illinois.

If valid, the effect of this objection, like appellants' apportionment objection, would be to require Illinois to measure the tax on the basis of something other than the cost of the call to a customer. This objection is, however, not valid. First, taxation on the basis of the value or cost of the taxed good or service is commonplace and has never been thought to be unconstitutional simply because part of the value being taxed derives from economic activity in other states. If appellants' position were correct, the entire foundation for sales, use, gross receipts and other common types of state taxes would crumble. For example,

a sales tax—indeed the instant tax is functionally indistinguishable from a sales tax on long-distance interstate telephone calls—unquestionably can apply to goods purchased outside the taxing state yet be measured by the amount of the sale. This is true even though the "services" provided by the taxing state bear little direct relation to the cost or value of the goods sold.

Second, the taxpayer is in Illinois during the telephone call which provides the basis for tax. That person is, therefore, enjoying the benefits and privileges afforded by Illinois, such as fire and police protection. This alone is sufficient to satisfy the fair relation requirement.

Third, the challenged tax is not a user fee, like the highway taxes at issue in *American Trucking Associations, Inc. v. Scheiner*, ___ U.S. ___, 107 S. Ct. 2829 (1987). In such instances, it may be appropriate to require that the measure of the tax bear some relationship to the services provided by the State, but the same requirement is neither needed nor imposed for general revenue taxes.

In sum, Illinois has constructed a tax that apportions to the State no more than its fair share of the total universe of potentially taxable interstate transactions and that reasonably assures the taxpayer that his interstate calls will be free of any added tax burden attributable to the fact that state lines have been crossed. Moreover, including the tax on the bill sent to the person to whom the call is charged is by far the most practical means of levying and collecting a tax of this nature. No state imposes a tax using any of the absurd, impractical and constitutionally questionable means that would be necessary to satisfy appellants' demand for call-by-call apportionment.

ARGUMENT

The Act applies to "the act or privilege of originating in this State or receiving in this State interstate telecommunications" and is measured "at the rate of 5% of the gross charge for such telecommunications purchased at retail." Ill. Rev. Stat. ch. 120, para. 2004. According to the definition of "gross charge", found in Sections 2(a) and 2(b) of the Act, the tax is levied only upon "the amount charged to the taxpayer's service address in the State."

Nothing in the Commerce Clause prohibits a tax on interstate telephone calls. As this Court recently stated, "*Complete Auto* abandoned the abstract notion that interstate commerce 'itself' cannot be taxed by the States." *D. H. Holmes Co. v. McNamara*, No. 87-267, slip op. at 6 (U.S. May 16, 1988), 56 U.S.L.W. 4400. Indeed, appellants do not claim that Illinois may not tax interstate telephone calls, but rather appellants argue that the method Illinois has employed to exact its tax violates requirements designed to safeguard interstate commerce from unfair or discriminatory state taxation.

Commerce Clause jurisprudence has established four such requirements: (1) the taxing state must possess nexus; (2) the tax must be fairly apportioned; (3) the tax must not discriminate against interstate commerce; and (4) the tax must bear a fair relation to the taxpayer's activity in the state. *Complete Auto*, 430 U.S. at 279.

Appellants do not question that Illinois has nexus to tax interstate phone calls that involve a party in Illinois and are charged to an Illinois service address. They attack the Act because the interstate telephone calls subject to the Act are taxed on the entire cost of the call, rather

than some lesser portion.[3] This, it is claimed, makes the tax "completely unapportioned, . . . subjects the telecommunications to multiple state taxation, . . . increases as the State's contact with the telecommunication decreases, and . . . lays a heavier burden on interstate telecommunications than intrastate telecommunications." (Goldberg Brief at i.) Appellants insist that the only method of properly taxing the retail cost of any interstate call must involve the apportionment of the cost of each call among several states. The vice of appellants' argument is that the Constitution does not require any particular method of taxation and certainly not the one suggested by appellants. All that is required is that interstate commerce not be unduly burdened. The Act meets this important requirement because it satisfies the tests set forth in *Complete Auto.*

I. THE ILLINOIS TAX IS FAIRLY APPORTIONED.

The purpose of the apportionment requirement is to ensure that states taxing multistate activity do not allocate to themselves more then their fair share of that activity. This safeguards taxpayers engaged in interstate commerce from excessive tax burdens attributable to the fact that

[3] We accept for purposes of this discussion appellants' hypothesis that what is being taxed by Illinois is the interstate phone call itself, rather than its purchase in Illinois. As explained in the text, the tax is nevertheless fairly apportioned. As a matter of economic reality, however, it is the purchase that is taxed, since the tax in fact applies only to Illinois purchases (*i.e.*, to calls charged to an Illinois number). So viewed, there is no need to apportion the tax on a call-by-call basis, because the limitation to Illinois purchases accomplishes all of the purposes that the apportionment requirement is designed to accomplish, leaving to other states the unimpaired power to tax calls purchased there.

their activities take place in more than one state with sufficient nexus to impose a tax. Apportionment allows states to allocate among themselves the universe of activity being taxed.

The Act is fairly apportioned. First, it taxes only a fair portion of the telephone calls that appellants claim Illinois has nexus to tax. Second, the Act is constitutionally indistinguishable from other taxes that have been approved by this Court. Third, the method of apportionment utilized by the Act is superior to any suggested by appellants. Lastly, the Act provides a credit which, in and of itself, acts as a method of providing fair apportionment.

A. The Act Taxes Only A Fair Portion Of Calls Touching Illinois.

It is fundamental to appellants' reasoning that any state in which a participant to a telephone call is located or through which an electronic telephone signal passes has nexus to tax some portion of the cost of that call. The Act apportions the universe of telephone calls that are potentially available to Illinois for taxation by taxing only those telephone calls that include an Illinois participant who charges the telephone call to an Illinois service address. This means that Illinois does not tax calls that include Illinois participants but are charged to a service address in another state, or calls that are transmitted through Illinois but do not include an Illinois participant. The fact that Illinois taxes only a portion of the telephone calls which it has nexus to tax, demonstrates that the Act is apportioned.

The fairness of the method of apportionment chosen by Illinois is demonstrated by the fact that it passes both

the internal consistency test and the external consistency test described in *Armco, Inc. v. Hardesty*, 467 U.S. 638 (1984) and *Container Corp. of America v. Franchise Tax Board*, 463 U.S. 159 (1983). The Act passes the internal consistency test because if the same statute were passed in every state, no interstate telephone call would be taxed more than once. Moreover, the external consistency test is met unless the appellant makes a showing that the method of apportionment is out of all proportion to the activity being taxed and thereby creates grossly distorted results. No such showing has been made or even offered by the appellants.[4] The Act is, therefore, fairly apportioned.

B. The Act Has The Same Economic Effect As Other Taxes Which Have Consistently Been Regarded By This Court As Fairly Apportioned.

Other taxes, including sales, use and gross receipts taxes, have consistently withstood constitutional scrutiny. These taxes are imposed on activities that are inextricably linked to interstate commerce and are apportioned among the states, not on a transaction by transaction basis, but on the basis of where sales are made. The practical effect of the Act is the imposition of a tax equal to 5% of the retail purchase price of an interstate telephone call charged in Illinois. As such, it is functionally indistinguishable from the sales, use and gross receipts taxes previously upheld by this Court. It should be evaluated in the same manner.

[4] The internal consistency test and external consistency test have been used to test fair apportionment and discrimination. Internal and external consistency are discussed in greater detail below. See pp. 30-33 *infra*.

The functional equivalence of the Act to sales, use and gross receipts taxes overshadows the various characterizations which the appellants have attempted to affix to the Act. This Court has consistently held that it is the practical effect of a state tax that determines its constitutionality, and not the labels used by the state statute, the lower courts or the litigants. *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977); *Commonwealth Edison Co. v. Montana*, 453 U.S. 609, 615-16 (1981); *American Trucking Ass'ns v. Scheiner*, ___ U.S. ___, 107 S. Ct. 2829, 2846 (1987). In other words, the Act should be judged on what it does and not what it is called.[5]

In *Wisconsin v. J. C. Penney Co.*, 311 U.S. 435 (1940), the Court was faced with a Wisconsin dividend tax on shareholders of corporations doing business in Wisconsin. The Wisconsin Supreme Court held that because the process of declaring dividends and the details of their distribution took place outside of Wisconsin, the tax was an unconstitutional attempt to tax activity beyond Wisconsin's borders. The Court reversed and stated that:

> Had Wisconsin . . . provided for a supplementary tax on the Wisconsin earnings of such corporations, but postponed liability for the tax until such earnings were to be paid out in dividends, the power of Wisconsin to do so would hardly be questioned.

[5] The Illinois Supreme Court's statement that the taxable event is not a "retail purchase" (Goldberg J. A. at 9a) does not preclude evaluating the tax in light of its retail purchase characteristics. The Illinois Supreme Court's comment concerning retail purchase simply indicated that it recognized that "the taxable event is linked inextricably to interstate activity" and, therefore, would not be immune from Commerce Clause scrutiny. (Goldberg J. A. at 9a.)

The Court continued:

> The case thus reduces itself to the inquiry of whether Wisconsin has transgressed its taxing power because its supreme court has described the practical result of the exertion of that power by one legal formula rather than another—has labeled it a tax on the privilege of declaring dividends rather than a supplementary income tax .... But the descriptive pigeon-hole into which a state court puts a tax is of no moment in determining the constitutional significance of the exaction.

Id. at 442-43.[6]

When the Act is viewed in light of its practical economic effect, it is no different than other types of taxes which have withstood challenge on Commerce Clause grounds. Sales taxes, which most closely resemble the Illinois tax, have consistently satisfied principles of fair apportionment.[7] In *McGoldrick v. Berwind-White Coal Mining Co.*, 309 U.S. 33, 58 (1940), the Supreme Court upheld a New York sales tax on goods shipped from outside of New York. This Court specifically rejected an argument that the tax should be held unconstitutional because it was unapportioned.

Similarly, use taxes, measured by the cost of items used within a state, have withstood Commerce Clause scrutiny.

[6] *Holmes*, No. 87-267 (U.S., May 16, 1988), does not undercut the principle advanced in *J. C. Penney*. In *Holmes*, this Court properly deferred to the Louisiana court of appeals' determination that certain activity was subject to Louisiana's use tax. *Holmes* does not restrict this Court's ability to look at the economic substance of a tax in evaluating it for Commerce Clause purposes.

[7] Indeed, if one postulates an Illinois sales tax applicable to the purchase of telephone calls, it would operate in exactly the same manner as the Act.

Just last term, in *Holmes*, this Court held that a Louisiana use tax on catalogues was fairly apportioned. The Louisiana tax was based on the full value of goods which were manufactured and purchased in another state and mailed from that state into Louisiana for use in Louisiana.

Taxes based on gross receipts that are allocated among the states based on where the gross receipts are earned have also been sustained without requiring apportionment of each transaction among several states. In *Standard Pressed Steel Co. v. Washington Dep't of Revenue*, 419 U.S. 560 (1975), this Court recognized the validity of apportionment based on sales to local consumers and stated:

> In the instant case, as in *Ficklen v. Shelby County Taxing District*, 145 U.S. 1, 12 S.Ct. 810, 36 L.Ed. 601 (1892), the tax is on the gross receipts from sales made to a local consumer, which may have some impact on commerce. Yet as we said in *Gwin, White & Prince, supra*, 305 U.S., at 440, 59 S.Ct., at 328, in describing the tax in *Ficklen*, it is "apportioned exactly to the activities taxed," all of which are intrastate.

419 U.S. at 564.

More recently, in *Tyler Pipe Industries, Inc. v. Washington State Department of Revenue*, ____ U.S. ____, 107 S.Ct. 2810, 2822 (1987), this Court stated that a form of gross receipts tax imposed by Washington did not violate the fair apportionment standard for failure to allocate or apportion between the state of wholesaling and the state of manufacturing.

If Illinois had enacted a gross receipts tax on carriers that supply interstate telephone services and had apportioned that tax by sales, the tax would satisfy constitutional apportionment standards. In *Moorman Mfg. Co. v. Bair*, 437 U.S. 267 (1978), the Court upheld an in-

come tax apportioned by sales within a state, and observed that:

> [I]t is evident that appellant would have had no basis for complaint if, instead of an income tax, Iowa had imposed a more burdensome gross-receipts tax on the gross receipts from sales to Iowa customers.

Id. at 280. While the legal incidence might be different, the practical economic effect of the Act would be virtually the same if the tax were imposed on the Illinois gross receipts from interstate calls of carriers such as GTE rather than on the cost of those same calls to the parties who charged them to their Illinois service addresses.

For Commerce Clause purposes, the Act should not be treated differently than the sales tax in New York on goods produced elsewhere, the use tax in Louisiana on catalogues produced and shipped from out of state and the gross receipts tax in Washington on revenue derived from goods manufactured out of state and shipped for sale and delivery in interstate commerce. The Act's method of apportionment is consistent with this Court's view of the Commerce Clause as it is applied to a wide range of state taxes.

C. The Constitution Does Not Mandate The Selection Of A Particular Method Of Apportionment. The Act Selects A Method Superior To Any Suggested By Appellants.

Illinois' method of apportionment works by allocating to the State only its fair share of the total set of potentially taxable calls and applying the tax to the full value of those calls. There is no evidence that the method adopted by Illinois will generate any revenue beyond that which would be derived if each telephone call were apportioned individually. Consider the set of two-party interstate calls

between persons in Illinois and persons in Indiana. It can reasonably be predicted that approximately one-half of those calls will be charged to service addresses in Illinois, the other half to service addresses in Indiana. As a result, the Act will be applied to approximately 50% of Illinois-Indiana interstate calls—an outcome functionally indistinguishable from that produced by a tax that apportioned each individual two-party call half to Illinois and half to Indiana. There is no difference between taxing 50% of all calls including an Illinois participant based on 100% of the charge and taxing 100% of the calls involving Illinois participants based upon 50% of the charge. Illinois has chosen one method of apportionment available to it. Given the purposes of the apportionment requirement—to give each state the opportunity to tax its fair share of multi-state transactions, while protecting the taxpayer involved in interstate activities from multiple tax burdens—there is no reason to require an alternative method of apportionment merely because it too may produce a fair result.

Apportionment of individual transactions is not mandated when the method of apportionment selected by a state yields a fair result. This common-sense conclusion is confirmed by decisions of this Court which have allowed different apportionment methods to exist side-by-side and have upheld formula apportionment in lieu of transactional accounting. See *Moorman*, 437 U.S. at 273 (1978); *Container Corp. of America v. Franchise Tax Bd.*, 463 U.S. 159, 164-65 (1983). Appellants' briefs, while replete with citations to cases that stand for the non-controversial generality that taxation of multistate activities must be fairly apportioned, cite not a single precedent, holding or suggestion that transaction by transaction apportionment is generally required by the Commerce Clause.

Once deprived of the opportunity to insist on apportionment of individual transactions, appellants' non-apportionment argument collapses. Moreover, there is no reasonable or practical method to implement transaction-by-transaction apportionment. Any practical means of apportionment must recognize and follow the attributes of the activity being taxed. As amicus MCI points out, there is no way to routinely record the particular route an interstate telephone call takes when moving from state to state. MCI further points out that it is impossible to meaningfully apportion the charge for a particular call among the States. Moreover, "the very number of calls involved demonstrates that, even if it were technically feasible to record and analyze routinely the routing of every call, the time, equipment, and expense involved for the carriers would be enormous." (MCI Brief at 2.)

When viewed against the real world, the methods of transaction by transaction apportionment that are implicitly suggested or explicitly endorsed in appellants' briefs are no more effective in avoiding multiple tax burdens and are either legally questionable or exceedingly impractical, if not impossible, to implement.

1. Mileage Apportionment Is Legally Suspect And Practically Impossible.

One proposal suggested at various places in appellants' briefs is that the cost of a call should be apportioned on the basis of the mileage between the callers' locations. This notion is not feasible. It would mean, for example, that 90% or more of a call between Illinois and California would have to be allocated for taxation by Iowa, Nebraska, and other intervening states. As amici MCI and the National Conference of State Legislatures et al. point out,

there may be no intervening states. Moreover, because electronic messages do not travel from one caller to another on a direct, horizontal line, and because the route taken by a telephone call varies each time a call is made, mileage apportionment becomes a practical nightmare. (MCI Brief at 1-2; National Conference Brief at 5-10.) Appellants' suggestion of mileage apportionment is a chimera.

MCI's description of switching systems shows that the route a call takes is controlled by elaborate computer programs that are generally designed to maximize, on a call-by-call basis, elements such as line quality, consistency, response time, and connection speed. In addition, once a route is chosen, the call may travel over any combination of media including microwave relay, fiber optic cable, satellite systems, or traditional telephone lines. In a satellite transmission, a signal may be beamed from a ground station in one caller's state to a satellite and back to a ground station in the second caller's state. In such transmissions, the country may be spanned but no signal will travel in the territory of any state between the eastern and western seaboards. Even when the signal proceeds through the air by a series of microwave relays, the routing could be quite circuitous, so that the states through which the microwaves pass cannot be determined by looking at a map or by any other consistent reliable means. (MCI Brief at 1-2.) Thus, appellants' implicit suggestion that mileage or distance is an appropriate method of apportionment is destroyed when one recognizes that a tax based on mileage and imposed by the originating, receiving or intervening states is an impossibility to administer.

Further, limited contact between the telecommunication and the intervening states makes it uncertain whether the intervening states would possess nexus to tax the call at

all, let alone to take the lion's share. See *Northwest Airlines, Inc. v. Minnesota,* 322 U.S. 292, 302-304 (1944) (Jackson, J., concurring) (no nexus to impose property tax on aircraft that pass through super adjacent airspace); 1 J. Hellerstein, *State Taxation* ¶ 10.2[6] at 646 (1983). Accordingly, the result of a mileage or distance apportionment formula could well be that *no* state would be able to tax most of the cost of a typical interstate call. Such an outcome might be convenient in insulating telecommunications from taxation, but it surely cannot be required by the Constitution.[8] It is no coincidence that appellants could not find a single state that has ever attempted to tax an individual interstate telecommunication on the basis of its geographical location along the route of the communication. (See GTE Brief App. at 1a-3a.)

2. Mileage Apportionment Is Not Mandated By Prior Court Rulings.

Central Greyhound Lines v. Mealey, 334 U.S. 653 (1948) and *Michigan-Wisconsin Pipeline Co. v. Calvert,* 347 U.S. 157 (1954) are the only cases cited by appellants that could be thought to support their position that apportionment based on distance or mileage is required by the Constitution in this case. Neither case has been much cited by this Court in its subsequent decisions, and both cases

[8] As the Court stated in *Complete Auto*:

> It might also be argued that adoption of a rule of absolute immunity for interstate commerce (a rule that would, of course, go beyond *Spector*) would relieve this Court of difficult judgments that on occasion will have to be made. We believe, however, that administrative convenience, in this instance, is insufficient justification for abandoning the principle that "interstate commerce may be made to pay its way."

430 U.S. at 289 n.15.

seem to rely on out-dated hypertechnical principles of Commerce Clause jurisprudence. In addition, each is distinguishable from the instant case.

Central Greyhound involved a tax on gross receipts from the sale of tickets on trips between cities in New York State, when the buses passed through, and made intermediate stops at, points in Pennsylvania and New Jersey. The Court held that New York could not tax the entire receipts from such trips, because such a tax would create the risk of multiple taxation if the intervening states, which were recognized to have tax nexus, also taxed their "share" of the same receipts. Instead of taxing the entire revenues from this travel, New York had to be satisfied with an apportioned share.

Central Greyhound's holding has limited usefulness. The mileage apportionment used in *Central Greyhound* cannot be readily applied to other means of conveyance or communication. In *Pan American World Airways, Inc. v. Virgin Islands,* 459 F.2d 387 (3d Cir. 1972), the plaintiff sought to have the court declare that the Virgin Islands' gross receipts tax as applied to an international air carrier was an unapportioned gross receipts tax and, therefore, a violation of the Commerce Clause. The Virgin Islands imposed a tax of 2% of the gross receipts from all tickets sold in the Virgin Islands and 2% of all revenues received in the Virgin Islands for carriage of baggage or freight irrespective of origin and destination of such traffic. The plaintiff relied principally on *Central Greyhound* to support its contention that mileage within the territory versus total mileage was the only permissible allocation formula. A mileage based formula would have yielded a tax equal to about 10% of the tax actually imposed. The Court of Appeals distinguished *Central Greyhound* stating that *Central Greyhound* "is no authority

for the proposition that allocation based on mileage is the only permissible form of allocation." *Id.* at 394. The Court of Appeals held that the tax was constitutional.

Given the nature of interstate telecommunications, mileage is not a suitable method of apportionment. Simply put, telecommunications are not at all like the passage of a bus along a highway. There is only the most ephemeral connection, if any, between geographically intervening states and the passage of the electronic signal from the telephone in Illinois to the telephone in California.

The tax at issue in *Michigan-Wisconsin Pipeline Co. v. Calvert,* 347 U.S. 157 (1954) was criticized because an artificial event, the "first taking" of gas, was created in order to tax the transportation of gas through a pipeline. The Court found that a similar artificial event could have been created by each state that the gas passed through. The case has no application here. Illinois taxes the origination or receipt of a telephone call charged to an Illinois address—a real event that takes place millions of times a day. The Act does not depend upon a legislative construct which can be duplicated by all of the states along the path of a telephone call. *Michigan-Wisconsin* is not a bar to the Illinois tax because Illinois taxes an actual event. It does not attempt to create an artificial event that would allow Illinois to tax the entire value of all interstate calls which pass through or into Illinois.

3. Imposing A Tax On Each Participant To A Telephone Call Is Not Constitutionally Mandated.

Contrary to appellants' position, the Constitution does not require apportionment on a transaction by transaction basis. See *Container Corp. of America v. Franchise Tax Bd.,*

463 U.S. 159, 164-65 (1983).[9] Illinois has selected a method of apportionment that is fair and that works. Alternatives that can be imagined seem plainly inferior to, and certainly are no better than, the Illinois apportionment method.

Consider call-by-call apportionment such as appellants seem generally to insist is constitutionally required. GTE claims to have the capability to "bill more than one state's tax on one bill for the same phone call." (GTE Brief at 32 n.13.)[10] Thus, it apparently proposes to compute, assess, itemize and collect from the party to whom the call is charged, and remit to each participant's state, the amount representing its apportioned share of the total. In the case of appellants' hypothetical 12-party conference call (Goldberg Brief at 30), the bill to the charged party—which would indeed be a formidable document—would show the tax from each of those states.

Even if technically possible, this system seems highly impractical, does no better than the challenged Illinois tax in distributing fair tax shares among the states, and raises

[9] The Goldberg appellants quote out of context a statement in *Mobil Oil Corp. v. Comm'r of Taxes,* 445 U.S. 425, 444 (1980), that would appear to suggest that *allocation* of potentially taxable transactions among the various states with tax nexus might be "incommensurate" with an *apportionment* process. (Goldberg Brief at 17 n.10; see also GTE Brief at 28.) But the question under discussion in *Mobil* was whether a state could allocate to itself *all* dividend income from business transacted in various states. Illinois does not allocate to itself all revenues from Illinois-linked calls.

[10] The quoted language does not say that GTE is capable of billing a tax to any participant other than the participant paying for the call. Nor does it suggest that GTE is capable of performing any of the sophisticated apportionment schemes to which appellants allude in their briefs. The only real evidence of GTE's capabilities in this regard is its apparent inability to add 5% to its customers' bills for interstate telephone calls for a period of several months. (GTE Jurisdictional Statement at 6.)

serious constitutional questions. In the case of a hypothetical call between Illinois and California, it is questionable whether California would have nexus to tax the Illinois party. See *National Bellas Hess, Inc. v. Dep't of Revenue*, 386 U.S. 754 (1967) (no nexus to collect the use tax from seller whose only connection with taxing state was through mail and common carrier). The nexus problem could be avoided by a modified version of this split-tax approach under which each participant to the call would be taxed by his own state. Suppose that a hypothetical call between Illinois and California cost $2.00, and that both States imposed a 5% tax on their apportioned share—$1.00 each. If the call were charged to the Illinois caller, his bill would be $2.05; the California participant would receive a bill for $.05 California tax.

It seems beyond question that such a scheme would produce objections from many quarters, including GTE and other carriers, since this split billing would be difficult or impossible to administer. Moreover, the scheme would be unfair to recipients of unwanted long-distance calls—for example a long-winded sales pitch from someone in a distant state attempting to sell "choice parcels" of desert real estate—who would be forced to pay tax on such calls. The Constitution may permit such a taxing arrangement, but it seems hard to believe that it requires it, especially when the current Illinois approach produces equally fair results. Again, appellants cannot point to a single state that pursues any of these forms of call-by-call apportionment.

The Goldberg appellants point to other states' "efforts to avoid multiple taxation" as being superior to the Illinois approach. (Goldberg Brief at 29.) But the examples they give do not support their conclusion. Florida's tax on *privateline* communications must use a different

method of apportionment because there is no separate charge for individual calls; significantly, where individual calls are separately charged and can be allocated among the states involved, Florida apparently employs the same apportionment system as Illinois. (See GTE Brief App. at 1a.) As for Virginia's use of circuit capacity as a means of apportioning its gross receipts tax, there has been no showing whatsoever that this is any better than an apportionment based on where individual calls are charged. As *Moorman* and *Container Corp.* make clear, the Constitution does not put this Court in the business of choosing among generally fair methods of apportioning taxes. That job, if it needs to be done, is for Congress and the state legislatures.

D. The Credit Provided By The Act Also Satisfies The Apportionment Requirements.

The method of apportionment used by Illinois—allocating the interstate call to the state in which it is charged—is entirely fair and fully satisfies all Commerce Clause policies. Although Illinois is under no constitutional obligation to provide any credit for taxes on the same call which other jurisdictions may seek to impose under different taxing schemes, Illinois does, in fact, provide a credit.[11] Persons such as appellants Goldberg and McTigue run no risk of being compelled to pay tax on more than the full cost of any call they may make. In *Holmes*, the Supreme Court expressly recognized that such a credit scheme,

[11] The credit mechanism becomes significant when, as in *Tyler Pipe*, a tax is not otherwise internally consistent. But if a tax is internally consistent, the credit should be wholly unnecessary to sustain its validity. The Act is internally consistent. See *infra* pp. 30-32.

identical to the one used in the Act provides, in and of itself, proper apportionment:

> The Louisiana taxing scheme is fairly apportioned, for it provides a credit against its use tax for sales taxes that have been paid in other States. See La. Rev. Stat. Ann. § 47:303(A) (West 1970) ("[a] credit against the use tax imposed by this Chapter shall be granted to taxpayers who have paid a similar tax upon the sale or use of the same tangible personal property in another state"); § 47:302(A)(2) (instructing that "there shall be no duplication of the tax"); § 47:321(A)(2) (West Supp. 1988) (same). Holmes paid no sales tax for the catalogs where they were designed or printed; if it had, it would have been eligible for a credit against the use tax exacted.

Slip op. at 6-7.

Appellants, whose briefs were filed before *Holmes* was decided, attack the credit provision because it applies only to taxes paid by the Illinois taxpayer, and not to those paid by others. In *Holmes*, the Louisiana credit was available only to the taxpayer and was nevertheless found to be a satisfactory method of apportionment.

II. THE DISCRIMINATION THAT THE COMMERCE CLAUSE GUARDS AGAINST IS PENALIZATION OF COMMERCE FOR CROSSING STATE LINES. THE ILLINOIS TAX IS INTERNALLY AND EXTERNALLY CONSISTENT AND PRODUCES NO IMPERMISSIBLE DISCRIMINATION.

Both appellants argue that the Act impermissibly discriminates against interstate commerce. (Goldberg Brief at 30-33; GTE Brief at 33-47.) The appellants support their argument by examples of telephone calls which involve in-state and out-of-state participants. The appellants' position is that discrimination has occurred because an in-state call with a cost equal to an interstate call will be taxed an equal amount. The argument is without support in law. The discrimination the Commerce Clause is designed to prevent is a penalty for crossing state lines and although the cost of a long-distance call is in part a function of distance, there is no evidence that it has anything to do with crossing state lines.

In *Commonwealth Edison Co. v. Montana*, 453 U.S. 609 (1981), this Court recognized that taxes which impose the same rate without regard to whether the transaction crosses state lines do not result in discrimination.

> [T]he Montana tax is computed at the same rate regardless of the final destination of coal, and there is no suggestion here that the tax is administered in a manner that departs from this evenhanded formula.
>
> * * *
>
> The premise of our discrimination cases is that "[t]he very purpose of the Commerce Clause was to create an area of free trade among the several States." Under such a regime, the borders between the States are essentially irrelevant. As the Court stated in *West v. Kansas Natural Gas Co.*, 221 U.S. 229, 255, 31 S.Ct. 564, 571, 55 L. Ed. 716 (1911), " 'in matters of foreign and interstate commerce there are no state lines.' "

Id. at 618-19 (citations omitted).

Faced with Illinois' evenhanded tax on both interstate and intrastate telephone calls, appellants make a discrimination argument based on a series of hypothetical telephone transactions. For example, the Goldberg appellants pose a hypothetical in which two calls are made from Chicago, one to Joliet, Illinois, and one to Gary, Indiana, each of which costs $2.00. (Goldberg Brief at 31.) They suggest that because each of the two calls bears the same ten cent tax and because the in-state call has two partici-

pants in Illinois and the interstate call has only one participant in Illinois, unlike subjects are being treated equally. They then argue that such equal treatment of unlike subjects is discriminatory. But, of course, not all calls between Chicago and Gary are charged to a Chicago number. The logically correct analysis thus requires the inclusion of the reciprocal calls from Joliet to Chicago and from Gary to Chicago. On the average, each call between Joliet and Chicago would be subject to a ten cent tax. On the other hand, on the average, each call between Gary and Chicago would be subject to a five cent tax. This is the case because approximately one-half of the calls would be from Chicago to Gary and would be taxed at the rate of ten cents per call, and approximately one-half of the calls would be from Gary to Chicago and would not be taxed at all. Thus viewed there is no discrimination.

The Goldberg appellants' other hypothetical compares calls of the same duration, one within Illinois and the other between Chicago and Los Angeles, and contends that, because the charge on the latter will be greater, this indicates discrimination against the interstate call. (Goldberg Brief at 31-32.) This argument seems principally to belong in the discussion of "fair relation" since it is really an attack on the notion that the cost of a taxed item is a proper basis for measuring the tax. The issue of fair relation is addressed at pp. 33-36 *infra*. The problem is not really one of discrimination against interstate commerce. For example, a call from Chicago to Carbondale may cost more and, therefore, could be more heavily taxed than one from Chicago to Gary. Thus, the cost of a long-distance call is in part a function of distance, but there is no evidence that the cost has anything to do with crossing state lines.

GTE suggests both hypothetical and actual taxes that are imposed on calls "billed or paid" within the taxing jurisdiction. (GTE Brief at 35-36.) GTE then considers the effect of such taxes on a call that is charged to an Illinois service address but billed to an address in one of the "billed or paid" jurisdictions, arguing that the taxation of such calls by both jurisdictions creates an unlawful multiple tax burden. Because the vast majority of calls are charged and billed to the same number, GTE's argument is of no real significance.

Moreover, GTE's argument (as well as that of the Goldberg appellants) wholly overlooks the significance of the holding in *Moorman Manufacturing Co. v. Bair*, 437 U.S. 267 (1978). Unlike the strained, largely imaginary, and totally insignificant multiple tax burdens that GTE conjures up, the one-factor Iowa apportionment formula upheld in *Moorman* created actual multiple tax burdens for some taxpayers when juxtaposed with traditional three-factor formula used by most other jurisdictions. The Court nevertheless found no violation of the Commerce Clause. The Court stated:

> [S]ome risk of duplicative taxation exists whenever the States in which a corporation does business do not follow identical rules for the division of income. Accepting appellant's view of the Constitution, therefore, would require extensive judicial lawmaking. Its logic is not limited to a prohibition on use of a single-factor apportionment formula. The asserted constitutional flaw in that formula is that it is different from that presently employed by a majority of States and that difference creates a risk of duplicative taxation. But a host of other division-of-income problems create precisely the same risk and would similarly rise to constitutional proportions.
>
> Thus, it would be necessary for this Court to prescribe a uniform definition of each category in the

three-factor formula. For if the States in which a corporation does business have different rules regarding where a "sale" takes place, and each includes the same sale in its three-factor computation of the corporation's income, there will be duplicative taxation despite the apparent identity of the formulas employed. A similar risk of multiple taxation is created by the diversity among the States in the attribution of "nonbusiness" income, generally defined as that portion of a taxpayer's income that does not arise from activities in the regular course of its business. Some States do not distinguish between business and nonbusiness income for apportionment purposes. Other States, however, have adopted special rules that attribute nonbusiness income to specific locations. Moreover, even among the latter, there is diversity in the definition of nonbusiness income and in the designation of the locations to which it is deemed attributable. The potential for attribution of the same income to more than one State is plain.

Id. at 278-279. (footnotes omitted)

The essence of the holding in *Moorman* is that a tax apportioned according to where sales are made will not violate the Commerce Clause even though some taxpayers suffer multiple tax burdens because of the interaction of the tax with a different tax of another state.

In addition to the basic requirement that statutes not discriminate on their face, recent Supreme Court opinions have demanded that state taxes be internally consistent so as to avoid discrimination against interstate commerce. The doctrine of internal consistency requires that if the tax at issue were imposed by each state, interstate commerce would be subjected to no greater burden than intrastate commerce.

The Act passes this test of internal consistency. If every other state adopted the same tax, no call would be taxed more than once, because the tax applies only to calls charged to a service address in the taxing state. Appellant GTE's attempt to avoid this conclusion is disingenuous. (GTE Brief at 26-29.) Seizing on the phrase "like tax" in *Armco, Inc. v. Hardesty*, 467 U.S. 638, 644-45 (1984), GTE posits that other states might adopt taxes generally similar to, but in significant respects different from, the Illinois tax. Insofar as these hypothetical taxes differ from one another, GTE points out that those differences might produce multiple taxation of particular taxed transactions.

This "reasoning" totally defeats the logic of the internal consistency principle. Indeed, whenever there is more than one fair method for taxing a transaction, no method could ever pass GTE's reformulation of the internal consistency standard, because it is the differences in the various methods of taxation that produce the theoretical possibility of multiple taxation.[12] In order for internal consistency to be an effective litmus test, it must be assumed that other states adopt a tax identical to the challenged tax.

The constitutionality of the Illinois tax under the internal consistency test should be compared with the failure under the internal consistency test of the tax at issue in *American Trucking Ass'ns, Inc. v. Scheiner*, ___ U.S. ___, 107 S.Ct. 2829 (1987). In *American Trucking*, this

[12] If GTE's reformulation of the internal consistency test had been applied in *Moorman* or *Container Corp.*, the taxes in both cases would have failed the test. Indeed, given the infinite number of methods of income tax apportionment which can be conceived of, it is difficult to imagine an income tax which would satisfy the GTE reformulation of the internal consistency test.

Court held unconstitutional certain flat taxes on trucks which traveled in the Commonwealth of Pennsylvania because the Pennsylvania taxing scheme failed the internal consistency test. If the tax imposed by Pennsylvania were imposed in all fifty states, a truck which traveled in all states would pay fifty times more tax than a truck which stayed in Pennsylvania, even if each truck traveled the same number of miles. Therefore, the Pennsylvania statutes imposed an impermissible burden on interstate commerce. Conversely, if the Act were imposed in every state, a caller placing interstate telephone calls from each of the fifty states would pay exactly the same tax as a caller who placed interstate calls with identical charges exclusively from Illinois.

The Illinois tax is also externally consistent. Where the requirement of internal consistency is a matter of logic and structure, the external consistency principle is an empirical safety valve that empowers the Court to protect commerce against the effects of a tax that claims for the taxing state a share that is "out of all appropriate proportions to the business transacted . . . in that State," or leads to "grossly distorted result[s]" or is "outrageous in a particular case." *Container Corp.*, 463 U.S. at 170, 182-183 (citations omitted).

As *Container Corp.* makes clear, the burden of proving a lack of external consistency is on those who claim that a tax operates in an unfair or distorted manner. Here, an issue of external consistency might arise if it were shown that a highly disproportionate percentage of calls between parties in Illinois and parties in other states are charged to service addresses in Illinois. Appellants have made no allegation that such a state of affairs exists. Indeed, the individual appellants have not alleged that they have paid a penny more in tax than they would

have paid if, instead of taxing only those of appellants' interstate calls charged to their own numbers, the State had instead taxed an apportioned share of every interstate call in which appellants participated.

III. THE ILLINOIS TAX IS FAIRLY RELATED TO THE ACTIVITY OF THE TAXPAYER.

The tax at issue in this case is measured by the charge for the taxed transaction. This is the virtually uniform method by which transaction taxes, such as sales, use and gross receipts taxes are assessed. Appellants' suggestion that the Illinois tax violates the requirement of fair or reasonable relationship to the taxpayer's activities or presence in the state is an attack on this well established method of taxation.

Simply stated, appellants' objection is that the cost of the interstate call, which provides the measure of the tax, depends in part on the distance between the calling parties, whereas the services or protection afforded by Illinois to the Illinois caller and to the call itself do not so vary. They also point out that the percentage of the total mileage between participants in an interstate call that is in Illinois actually tends to vary inversely with the cost of the call. Even if accurate, these observations afford no grounds for invalidation of the tax.

Preliminarily, it can be noted that appellants' complaint would not be solved by the kind of call-by-call apportionment they elsewhere espouse. Whether Illinois were to tax 50% of each two-party interstate call (and 33% of each three-party call, etc.) or, as it now does, 100% of the subset of such calls that are charged to the Illinois party, the kind of relationship that appellants insist must exist between the State and the tax would be equally

lacking. In effect, appellants' fair relation challenge is no more than a revisiting of their apportionment argument.

The Constitution only requires that the tax imposed be fairly related to the activity of the *taxpayer* in the state imposing the tax. Here, the tax is related to the amount of calling activity of the taxpayer in Illinois. As was recognized in *Commonwealth Edison v. Montana*:

> When a tax is assessed in proportion to a taxpayer's activities or presence in a State, the taxpayer is shouldering its fair share of supporting the State's provision of "police and fire protection, the benefit of a trained work force, and the "advantages of a civilized society."

453 U.S. at 627.

The Constitution requires no direct link between state services and state taxes, except perhaps in the area of user charges such as were at issue in *American Trucking*. As the Court stated in *Commonwealth Edison*, 453 U.S. at 622-23 (1981) (citations omitted):

> [T]here is no requirement under the Due Process Clause that the amount of general revenue taxes collected from a particular activity must be reasonably related to the value of the services provided to the activity. . . . There is no reason to suppose that this latitude afforded the States under the Due Process Clause is somehow divested by the Commerce Clause merely because the taxed activity has some connection to interstate commerce; particularly when the tax is levied on an activity conducted within the State.

Commonwealth Edison states that the fourth prong of *Complete Auto* requires "that the *measure* of a tax must be reasonably related to the extent" of the taxpayer's presence or activities in the state. *Id.* at 626. Here, there

is at least one party, the taxpayer, present in Illinois for the duration of the taxed call, and, of course, the service address to which the call is charged is permanently located in Illinois. The tax is based upon the value the person charging the call to the Illinois number places on the telephone activity. It is measured by what he is willing to pay for the call. Nothing could be more closely related to the taxpayer's activity in Illinois. The fourth prong of *Complete Auto* is thus satisfied.

If appellants' argument on this point were correct, it would have drastic consequences for other types of taxes, such as those on sales, use or gross receipts, that are likewise measured by the cost of the goods or services sold. When someone buys a new automobile that has been manufactured outside the state, the in-state contribution will likely vary little whether the automobile is a Chevrolet or a Cadillac, but the sales tax will vary substantially. If the Court were to strike down the cost of the taxed telephone call as a proper measure of the tax (assuming, of course, that the tax does not discriminate against interstate commerce), it is hard to see how traditional sales taxes and other taxes that are similarly measured could survive.

Any uncertainty about this issue that may have existed at the time appellants prepared their briefs was put to rest by the decision in *Holmes*. There, the Louisiana use tax was measured by the cost to the appellant of the catalogues, which had been printed out of the State and, by the Court's hypothesis, were still a part of interstate commerce at the time they were taxed. Slip op. at 6. Louisiana's method of measurement of its use tax was subject to precisely the same objection made by appellants here, but the Court rejected the challenge:

> *Complete Auto* requires that the tax be fairly related to the benefits provided by the State, but that condition is also met here. Louisiana provides a number of services that facilitate Holmes' sale of merchandise within the State: It provides fire and police protection for Holmes' stores, runs mass transit and maintains public roads which benefit appellant's customers, and supplies a number of other civic services from which Holmes profits. . . . [T]he use tax paid by Holmes, on catalogs designed to increase sales, is related to the advantages provided by the State which aid appellant's business.

Slip op. at 7.

While the telephone calls taxed by Illinois are personal, as well as commercial, the ability to make these calls and to conduct any business is aided by Illinois in the same manner as the distribution of D. H. Holmes's catalogues was by Louisiana. It is plain, therefore, that the Illinois telephone tax is equally related to the taxed transaction as the Louisiana use tax was, and equally valid under the fourth prong of the *Complete Auto* test.

CONCLUSION

The judgment of the Supreme Court of Illinois should be affirmed.

Respectfully submitted,

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(11)

Nos. 87-826, 87-1101

In The

Supreme Court of the United States

October Term, 1987

JEROME F. GOLDBERG, ROBERT McTIGUE
and GTE SPRINT COMMUNICATIONS CORPORATION,
Appellants,

v.

ROGER D. SWEET, Director of the Illinois
Department of Revenue, and JEROME COSENTINO,
Treasurer of the State of Illinois,
Appellees.

On Appeal from the
Supreme Court of Illinois

REPLY BRIEF OF APPELLANT GTE SPRINT COMMUNICATIONS CORPORATION

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REPLY BRIEF OF APPELLANT
GTE SPRINT COMMUNICATIONS CORPORATION

Appellees and *Amici* Assert Newly-Raised "Facts" on Call Charging Patterns which only Confirm that the Tax is Unconstitutional

GTE Sprint introduced facts below never controverted by the State. Nor were those facts disputed by MCI when it challenged the tax and obtained judgment in the trial court on its claim that the Illinois tax violates the Commerce Clause. R. C 1044-46.[1] Yet, the State and MCI (ostensibly as "*amicus*") have presented several new "facts," in an attempt to elevate the charging of a call to an Illinois service address to a sale, billing, call-origination or other economically significant event which can support apportionment of the tax.[2] These newly-introduced "facts," regarding allegedly typical ways long distance calls are charged, cannot so transform the charge address, however, and merely confirm the tax is unconstitutional.[3]

Most significantly, MCI admits at the outset that:

> By customary usage in the industry, a "*service address" is the location of a telephone* or other telecommunications device *and is not necessarily the same as the address to which the bill is sent.* For exam-

[1] MCI now urges, as "*amicus*," that the Illinois tax *is* constitutional. But MCI should be estopped from so changing its position. *See, e.g., Allen v. Zurich Insurance Co.*, 667 F.2d 1162, 1166 (4th Cir. 1982). In addition, although the MCI position has been submitted as representative, AT&T and other carriers have challenged taxes very like the Illinois tax, as unapportioned and violating the Commerce Clause. *See* Plaintiffs' (AT&T's) Proposed Findings of Fact ¶¶ 37, 38 and 43, *American Telephone and Telegraph Company et al. v. District of Columbia*, C.A. 8599-87 and C.A. 10080-87 (Superior Ct. D.C. filed Oct. 7, 1987) in App. A hereto; *Green v. Warden, U.S. Penitentiary*, 699 F.2d 364 (7th Cir.), *cert. denied*, 461 U.S. 960 (1983) (judicial notice of pleadings permitted).

[2] The State's facts are improperly introduced here, so should be disregarded in any event. *See, e.g., Wisconsin Higher Education Corp. v. Bear*, 789 F.2d 577, 579 (7th Cir. 1986).

[3] The same may be said of the nearly-identical "facts" submitted by *amicus*, The National Conference of State Legislatures, *et al. See* Nat'l Conf. Br. at 4-10.

> ple, an individual with a telephone at his vacation home (the service address) might have the bills for that telephone sent to his primary residence (the billing address). Similarly, *a corporation with many offices might have the phone bills for all of them sent to its headquarters.*

MCI Br. at 4 (emphasis added). MCI thus admits that where a call is charged will not necessarily coincide with where that call is billed. The practice manual utilized by a GTE local exchange company confirms that, in the industry, the service address is the phone location and does not necessarily coincide with the billing address, which a customer arbitrarily selects.[4]

Other new "factual" assertions made by the State and MCI to identify the Illinois charge address with the call origination location are simply in error. For example, the State and MCI allege that, "typically" or "normally," a call originating in Illinois will be charged to an Illinois service address, which MCI identifies as the location of a telephone, but that a call terminating in Illinois will not be. State Br. at 3; MCI Br. at 4-5. But they so allege this pattern obtains without any substantiation. Indeed, MCI itself admits elsewhere that calls may originate and terminate in locations totally divorced from where the call is charged (*e.g.*, credit card calls). MCI Br. at 5.

Further, this Court may take judicial notice of the fact that the State's allegedly "typical" pattern is no pattern at all: Carriers like Sprint (competitors of AT&T) do not necessarily possess information on the location of phones used to make particular calls and do not use, as a consequence, a "service address" for charging or billing calls. Sprint's closest equivalent to a service address is the "bill

[4] *See* excerpts from *GTE Northwest Inc. Practice Service Office System Series* in App. B hereto. *Bethel Conservative Mennonite Church v. Commissioner*, 746 F.2d 388, 392 (7th Cir. 1984) (judicial notice of readily verifiable internal corporate documents permitted).

to" address, arbitrarily designated by the *customer* when the customer subscribes to Sprint service. In addition, even those carriers who might purchase "service address" billing services or information from the local exchange carriers are not compelled to do so, and some even bill through third-party vendors. There is simply no mandatory way for carriers to charge or bill their customers. It is impossible to conclude that there is any certainty that all calls charged (or billed) to Illinois will represent Illinois-originated calls, then.[5]

With similar lack of substantiation, the State claims that, within the "universe" of long distance calling, it can be "predicted" that one-half of calls originating/terminating in Illinois will be charged to an Illinois address, so that the Illinois tax is "apportioned" to half the Illinois calls, by virtue of this charging pattern. The State also alleges that the "majority" of calls are charged and billed to the same number, so that these are equivalent events. State Br. at 16-17, 27-28 and 29. Yet when Sprint's and other carriers' long distance calls are not charged to a service address, a "bill to" address is a matter of customer choice, and carriers can handle their charging and billing procedures in any way they choose, the State can make no claim that bill or "charge" locations will be split neatly between Illinois and the state on the other end of the call, nor that the "bill" and "charge" location will coincide, except serendipitously. *See* discussion *supra* and fn. 5.

The State and *amici* also cite a Department of Justice study to claim that the economic significance of out-of-state transmission activity to Illinois long distance phone calling is minimal. They make the claim, of course, because

[5] *See* Sprint Customer Order Form (App. C hereto); *Bethel*, 746 F.2d at 392 (judicial notice of corporate documents permitted). *See also* Report and Order, *In re Detariffing of Billing and Collection*, CC Docket No. 85-88 at 3-4, 9-11, 14-15, 22, 24-25, 27-28, released Jan. 29, 1986. *Finish Line Express, Inc. v. Chicago*, 72 Ill. 2d 131, 379 N.E.2d 290 (1978) (judicial notice of filed public documents permitted).

the Illinois tax ignores this out-of-state calling component. State Br. at 18-20; MCI Br. at 1-2; Nat'l Conf. Br. at 5-10. However, US Sprint's tariffs, filed with the Federal Communications Commission, reveal that carriers' tariffs and call charges do vary with the distance of the call. *See* Excerpts from US Sprint Tariffs, Tariff F.C.C. Nos. 1, 2 and 3 in App. D hereto.

In sum, the Illinois tax is simply not a tax on calls billed, sold, or originated in Illinois and, even if it could, the State cannot rely on the alleged external charging behavior cited to demonstrate that the tax is confined to such calls.[6]

ARGUMENT

I. The Illinois Tax Is Not Fairly Apportioned

A. The Limit of the Tax to Simply Less than All Call Charges Does Not Apportion It

The State argues that "[t]he fact that Illinois taxes only a portion of the telephone calls which it has nexus to tax, demonstrates that the Act is apportioned." State Br. at 11. If this were true, any interstate calling tax with an arbitrary limit (*e.g.*, every fourth call originated or received in the taxing state) could be apportioned. Likewise, an income tax on a multi-state business could be deemed "apportioned" if it were limited to some random portion of the taxpayer's business activities. Such a result would be absurd, however, and defies *Container Corp. of America v. Franchise Tax Board*, 463 U.S. 159 (1983) which demands that the

[6] The State also repeats, as a "fact," the Illinois Supreme Court's clearly erroneous conclusion that the Illinois tax covers Illinois originating/terminating interstate calls which are *billed* or *paid in Illinois*, trying to make the tax appear more akin to a traditional sales tax. State Br. at 4. But, clearly, the tax, as the State and MCI elsewhere admit, covers calls *even where they are billed or paid for outside Illinois.* State Br. at 9; MCI Br. at 4; *see also*, GTE Sprint Br. at 5, 10, 19, and 22.

apportionment mechanism confine the tax to some proxy for value obtained from the state. GTE Sprint Br. at 29-31.

B. The Tax Is Not Limited to Half of the Call Charges and, therefore, Is Not Apportioned by Such a Limit, Nor Could It Be

The State suggests that the Court consider *collective* call charging behavior in assessing apportionment of the tax. It "predicts," for example, that, as to Illinois-Indiana calls, "approximately one-half of those calls will be charged to service addresses in Illinois, the other half to service addresses in Indiana" so that the tax will be "apportioned" by this charging pattern to one-half of Illinois originating/terminating call charges. State Br. at 16-17. Yet *nothing* in the tax itself guarantees such an allocation of call charges. Further, GTE Sprint has demonstrated that, for some carriers, there is no "service address charge" but only a customer-chosen "bill to" location. Since the "bill to" address for these calls is arbitrary, any division of call charges or billings as the State describes could only be fortuitous. Moreover, even the unidentified carriers or taxpayers who might currently charge as the State suggests could change their billing systems or charging practices tomorrow. *See* discussion and fn. 5 *supra* at 3 and App. B and C hereto. Thus the State's dependence on arbitrary and unpredictable external charging/billing behavior to apportion the tax simply underscores the tax's unconstitutionality. *Tyler Pipe Industries, Inc. v. Washington State Department of Revenue*, — U.S. —, 107 S. Ct. 2810, 2819 (1987) (tax cannot meet Commerce Clause requirements fortuitously); *Halliburton Oil Well Cementing Co. v. Reily*, 373 U.S. 64, 76 (1963) (Brennan, J., concurring). GTE Sprint has proven the "charge" mechanism cannot save the tax.[7]

[7] *Maryland v. Louisiana*, 451 U.S. 725, 759-60 (1981) (party need only adduce facts to show tax is unconstitutional and need not demonstrate just *how* unconstitutional it is); *American Trucking Associations, Inc. v. Scheiner*, — U.S. —, 107 S. Ct. 2829, 2842 (1987) (tendency of tax to be unconstitutional invalidates it).

Worse, however, is the State's assumption that a division of call charges could ever operate to apportion the tax. As MCI admits, calls charged to an Illinois address may nevertheless still be billed and paid for outside Illinois, so the charge location is not the site of the call's sale. *See* MCI Br. at 4 and p. 2, fn. 4 *supra*. Nor does the location of the call "charge" identify Illinois costs incurred to provide the service, the location of Illinois participants, nor that part of Illinois transmission activity conducted to generate a call. MCI Br. at 4; GTE Sprint Br. at 25. The charge location simply does not correspond to the site of the economically significant components of interstate calling, and cannot serve to apportion the tax, under any circumstances. *See* GTE Sprint Br. at 29-31.

C. The Tax Cannot Be Compared to a Sales, Use or Gross Receipts Tax

Both courts below rejected the State's arguments that the tax is a sales or use tax, finding that the tax could not be construed as a tax on local activity. GTE Sprint Br. at 7-8, 17-23. The State now contends that the Illinois tax "is *functionally* indistinguishable from sales, use and gross receipts taxes previously upheld by this Court." State Br. at 12 and 13, fn. 5 (emphasis added). In doing so, the State simply fails to comprehend the monumental difference between the models it cites and the Illinois tax.

1. The Sales/Use Tax Model Is Inappropriate: The Illinois Tax Is Assessed on Multi-State Service with No Single Situs for Sale/Use and, unlike the Constitutional Sales/Use Taxes, Must Be Apportioned

In the post-divestiture world of interstate communications, the "sellers" of service are the carriers with facilities to provide calls in every state (or resellers who utilize such facilities). The service is provided and enjoyed by virtue of simultaneous multi-state activity. The bills for services may be sent to any location the customer

chooses and the customer may choose to pay anywhere. *See* GTE Sprint Jurisd. Statement at 3-5, App. C thereto; Goldberg Jurisd. Statement at 9a, 21a (court finds "[a] person . . . cannot make or receive an interstate telecommunication without activating and participating in a complex network of interstate transmissions. . ."); GTE Sprint Br. at 3-4, 7-8; App. B and C hereto, discussed at 3 and fn. 5 *supra*. There is thus no single *local* place for the seller to "sell" or for the buyer to "buy" or for the buyer to "enjoy" -- as with tangible goods -- so that a "local" tax may be levied on one of these events.

Because of this, the Illinois tax, even as limited to calls charged to an Illinois service address, in no way resembles either a sales or use tax on the *local* transfer or enjoyment of goods. Unlike a traditional sales tax, for example, the Illinois tax, acknowledging reality, specifically applies to calls which may be charged in Illinois but billed or paid out-of-state. GTE Sprint Br. at 5, 22 and 27, fn. 8; MCI Br. at 4. Indeed, if the State were correct in analogizing the Illinois tax to a "sales" tax, the *tax would fail, in any event*, because the tax, as drafted, would still cover calls purchased (billed/paid) outside Illinois. *McLeod v. J.E. Dilworth Co.*, 322 U.S. 327 (1944) (sales tax unconstitutional where it covers purchases occurring outside taxing state).

Nor can the tax resemble a use tax, when it is clear that the caller enjoys services outside the state even as he or she originates or receives a call in Illinois. Further, the call participant through whom a call is charged or billed may not even be in Illinois to make or receive a call charged there (as MCI admits). MCI Br. at 4. There is no altogether local Illinois "use" taxed here. *See* discussion *supra* at 6-7.

Ignoring these facts, the State cites a selection of inapplicable sales and use tax cases to argue that the tax is apportioned. For example, the State cites *McGoldrick*

v. Berwind-White Coal Mining Co., 309 U.S. 33 (1940) where the Court upheld a sales tax on the purchase of goods shipped from out-of-state. But the tax in *McGoldrick* was confined to a clear, traditional transfer of a tangible good in the taxing state because the sales office was located and receipt of contracts and delivery of goods took place in the taxing state. Thus, no apportionment was necessary.[8] Here, the tax is not confined to any such traditional local transfer because the billing and payment can occur outside Illinois.

Similarly, in *D.H. Holmes Co. v. McNamara*, — U.S. —, 108 S. Ct. 1619 (1988) the Court approved a Louisiana use tax on the distribution of mail order catalogs. There, however, the tax was strictly limited to the in-state distribution of catalogs (and therefore apportioned). *Holmes*, 108 S. Ct. at 1624. The same cannot be said here with regard to a service which is provided and concomitantly enjoyed by virtue of multi-state activities.[9] As are the sales and use taxes which they upheld, *McGoldrick* and *Holmes* are simply inapposite here.[10]

[8] Central to the outcome in *McGoldrick* was the fact that the taxed activity met traditional legal criteria for a local sale of goods. *McLeod v. J.E. Dilworth Co.*, 322 U.S. at 329 ("According to practical notions of what constitutes a sale . . . reflected by what the law deems a sale, [the taxed activity] constituted a sale in New York and accordingly we sustained a retail sales tax by New York").

[9] Other states have recognized that taxes on multi-state telecommunications service are fundamentally different from taxes on in-state sales or uses of tangible property. The Florida legislature, in fashioning a proposed service tax on telecommunications, devised six *different* methods for actually *identifying* the location of the "sale" or "use" of the interstate service. Only if Florida first qualified as the "sale" or "use" locale was the tax applied, and then only according to an apportionment formula. J. Mills, *The 1987 Legislative Session*, 1987 Fla. St. Univ. L. Rev. 607, 631-634 (1987).

[10] Likewise, in *Wisconsin v. J.C. Penney Co.*, 311 U.S. 435, 441-42, 443 (1940), dividends paid "out of income derived from property located and business transacted" in Wisconsin "calculated ac-

(Footnote continued on following page)

2. The Gross Receipts Tax Model Is Inappropriate: The Illinois Tax Does Not Have a Sales Apportionment Formula and Even If It Did, It Could Not Apportion the Tax

The State also mistakenly relies on *Standard Pressed Steel Co. v. Department of Revenue*, 419 U.S. 560 (1975), upholding Washington's business and occupation tax levied upon the gross receipts from sales of aerospace fasteners, and *Moorman Manufacturing Co. v. Bair*, 437 U.S. 267 (1978), upholding a net income tax. State Br. at 15; MCI Br. at 12. Both of these taxes were apportioned by being limited to an in-state percentage of total interstate sales of tangible goods. Here, however, the Illinois charged call limit is not a limit of the tax to calls "sold" in Illinois since those calls, though "charged" to an Illinois address, can be billed or paid elsewhere.

Even if the Illinois tax *were* limited to in-state sales, the *Standard* and *Moorman* cases would not control. Although in-state sales may reflect a fair in-state portion of interstate gross receipts or incomes, in-state sales of long distance calls cannot serve as a fair reflection of Illinois transmission, origination, termination, investment, costs or economic support which goes into interstate calling because the place of sale has no logical relationship to these activities or events. *See* discussion *supra* at 2-3, 5-7; GTE Sprint Br. at 29-31. Indeed, commentators have criticized *Standard* and *General Motors Corp. v. Washington*, 377 U.S. 436 (1964), upon which *Standard* relied, as having produced unsatisfactory results -- especially with regard to apportionment -- precisely because of the frequent inability of sales to reflect, in any economically realistic sense, the

[10] *continued*
cording to the . . . formula . . . employed in assessing the general corporate income tax. . ." were taxed. Thus, the tax "was [already] apportioned," unlike the Illinois tax. *See* State Br. at 13.

taxing state's contribution to multi-state activities.[11] Here, the fragmented "sales" locations do not reliably reflect the location of the economically significant components of interstate calling, so reliance upon *Standard* and *General Motors* is misplaced.[12]

D. The State's Administrative Inconvenience Argument Is Misdirected: The Arbitrary Limit of the Tax Is Not the Only Realistic Alternative to a True Apportionment Formula, as Other States' Formulas Show

The State argues that GTE Sprint has espoused "mileage-based" or "call-by-call" apportionment, but that such apportionment methods are too burdensome administratively and far inferior to the method employed by the Illinois tax. Thus, the State claims the Illinois method is the only apportionment alternative. State Br. at 16-17, 21. These attacks on straw men are misdirected. GTE Sprint has not argued that these methods of apportionment are the only acceptable ones by simply noting that the current tax ignores numerous significant economic components of interstate calling (such as transmission) or by showing that, on an individual call basis, the tax is not apportioned. *See* GTE Sprint Brief at 3-4, 30-31 and fn. 11.

Further, the State's contention that there is no calculable alternative to the tax's current "apportionment" method is demonstrably wrong. For example, it cannot be contro-

[11] J. Hellerstein, *State Tax Discrimination against Out-of-Staters*, 30 Nat'l Tax J. 113, 123 (1977) ("[T]he Washington business activities tax [at issue in both *General Motors* and *Standard*] ought to have been treated, not in the way retail sales tax cases have been decided, but as an excise on the privilege of doing business. Mr. Justice Brennan, therefore, was on impeccable ground in concluding in his dissent from . . . the *General Motors* case that the tax was unconstitutional for lack of apportionment").

[12] Some unapportioned "gross receipts" taxes have been upheld as taxes assessed "in lieu of" property taxes. The long distance carriers are already taxed on their Illinois property, however. Ill. Rev. Stat. ch. 120, §§ 482 *et seq.* (Supp. 1988).

verted that approximately sixty percent of long distance phone call costs derive from access charges assessed by the local exchange carriers for picking up and dropping off calls. Dept. of Justice, ***The Geodesic Network: 1987 Report on Competition in the Telephone Industry*** at 3.49 (1987); ***Finish Line Express, Inc. v. Chicago***, 72 Ill. 2d 131, 379 N.E.2d 290 (1978) (judicial notice of investigative reports of public agencies permitted). Any originating/terminating state might therefore "apportion" a tax on long distance calls by limiting it to thirty percent of the call charge which represents the economically-significant in-state pickup (or drop-off) cost of the call.

Other, more sensitive calibration is also possible. The State of Hawaii has passed a four percent excise tax on interstate and foreign telecommunications covering calls originating/terminating and billed in Hawaii, and the Hawaii Department of Taxation has developed, with the help of the industry, a proposed cost-based formula to apportion it. Hawaii Rev. Stat. § 237-13(6) (Supp. 1987); Hawaii Adm. Rules, Section 18-237-13(f) (1988) (proposed June 21, 1988) (published ***Honolulu Advertiser***, July 7, 1988, at D4, col. 1-3); *see* App. E and F hereto.[13] Additional states have apportioned their taxes on interstate telecommunications using other economically-sound factors: New York apportions its gross receipts tax on a property factor (N.Y. Admin. Code tit. 20, § 72-1 (1987)); Virginia apportions on the basis of circuit capacity (*see* Goldberg Br. at 29); and Wisconsin factors combined property and originating call revenue to do so

[13] Under this formula, if, on average, 30% of a carrier's overall costs on covered calls are attributable to Hawaii, the tax due for each call would be calculated as follows: Call charge × 30% (or whatever average percentage of overall costs are) × 4% tax rate = tax on gross income from such call. ***See also Roemer v. Board of Public Works***, 426 U.S. 736, 742 (1976) (judicial notice of state regulations); ***People v. Pollution Control Board***, 103 Ill. 2d 441, 469 N.E. 2d 1102, 1105 (1984) (judicial notice of proposed regulations).

(Wis. Stat. Ann. § 76.38 (West Supp. 1987)).[14] The State is simply wrong in suggesting "charge" apportionment is the only workable method, and must be accepted. *American Trucking Associations, Inc. v. Scheiner*, — U.S. —, 107 S. Ct. 2829, 2847 (1987) and fn. 27 (where other states have implemented alternative apportionment methods, argument that alternatives are impossible is baseless).

The experience in other states also proves that the actual assessment of taxes, using such alternative formulas, will pose no administrative burden. State Br. at 16-18 and 23. Businesses can and do assess taxes using such mathematically-devised formulas, applied to bills by computer. *See* R. Westphal, *The Computer's Role in Simplifying Compliance with State and Local Taxation*, 39 Vand. L. Rev. 1097 (1986). Further, contrary to the State's assertion, more sensitive alternative formulas are indeed "superior" to the Illinois example since the Illinois method is completely arbitrary while the other cited formulas utilize economically substantive *indicia* of Illinois contributions to interstate calling and would foreclose the substantial and non-incidental overlap in taxes which the Illinois tax creates. *Container*, 463 U.S. 159, 169 (1983); GTE Sprint Br. at 26-31.

E. *D.H. Holmes* Does Not Demonstrate that the Credit Provided in the Illinois Tax Can Apportion that Tax

The State, citing a statement from *D.H. Holmes Co. v. McNamara*, — U.S. —, 108 S. Ct. 1619, 1623 (1988) to the effect that the credit provision in a use tax can serve to "apportion" it, claims that the Illinois tax's credit provision likewise apportions the tax. But the tax in *Holmes*

[14] Even mileage apportionment formulas exist. Florida apportions its sales and gross receipts taxes on interstate private line telecommunications services using Florida mileage. GTE Sprint Br., App. A at 1a. The Florida tax on non-private line services does *not* utilize the Illinois approach. *See* GTE Sprint Br. at 36.

was confined to a local "use" -- the entirely in-state distribution of catalogs. Thus the only "apportionment" problem *Holmes* dealt with was the possible assessment, by another state, of a sales tax on the Louisiana-distributed but foreign-purchased catalogs. Louisiana therefore provided a credit for paid sales tax, to address residual multiple taxation which might arise from the unique collision of the legally "complementary" sales and use taxes.[15]

The *Holmes* credit mechanism served to solve an anomalous residual multiple tax problem, then. And it did so arbitrarily, by allowing the absolute amount of the paid sales tax to simply reduce or eliminate the use tax, without an attempt to divide the tax revenue between the taxing states according to the respective states' real economic contribution to the taxed activity. GTE Sprint Br. at 41-42, citing *Halliburton*, 373 U.S. 64, 76 (Brennan, J., concurring). That may have been an adequate solution with regard to use/sales taxes since there is simply no economically realistic way of determining what percentage of a taxed activity a "sale" represents, as opposed to a "use," as "sale" and "use" are not two aspects of seamless interstate activity. But this type of arbitrary credit cannot be deemed an adequate solution here, because, here, by contrast, an economically realistic division among the states of the seamless whole *is* possible. *See* discussion *supra* at 10-12.

Moreover, some realistic division among the states of such a seamless whole is *necessary*. If the *Holmes dicta* signifies what the State suggests, states could eschew apportioning taxes on unified multi-state activities, leaving

[15] These separate events -- sales and use -- have been considered legally equivalent tax events in order to prevent out-of-state purchases from escaping taxation because the taxing state would not have sufficient nexus to force the out-of-state seller to collect the tax. Here the carriers or "sellers" operate and can be required to collect tax everywhere. *See* GTE Sprint Br. at 3-4, 43.

to credit provisions the job of doing so. But, for these types of taxes, the credit simply could not shoulder the burden. Taking the example of the Illinois tax, credits would be necessary not on casual sales, but for vast numbers of incessant, individual telephone calls, on a monthly basis. In addition, nexus problems endemic to use tax assessment, and the consequent sporadic collection of these taxes, indicate that, realistically, use/sales taxes present a less-frequent need for a credit to cure overlap than that which would be presented by consistently-applied taxes on seamless interstate activity, like telecommunications.[16] Allowing the credit provision to "cure" the enormous apportionment problem posed by the Illinois tax (or an income tax on multi-state business) would do nothing but generate a dizzying round of chaotic credit proceedings which would crush both callers and other states with the cost and burden of dividing the tax among them.[17] Such a startling result cannot be the holding of *Holmes*.[18]

[16] *See, e.g.*, B. Henszey, *Use Tax Collection: Past, Present and Future*, 25 Am. Bus. Law J., 635-37 (1988); GTE Sprint Br. at 44. *See also* fn. 15 *supra* (states will have nexus to consistently require carriers to assess tax).

[17] To make matters worse, the credit system would be obliged to cure multiple taxation that results when another state assesses tax on the sale of access services, on a different taxpayer. Further, who will arbitrate which phone taxes can be credited against one another? The credit provision appears to be an unmanageable solution for these problems. *See* GTE Sprint Br. at 5, 37-38, 43.

[18] Indeed, sales/use taxes, as opposed to taxes on unified interstate activities (like the tax at issue here or a tax on multi-state income), pose no real apportionment problems:

> Where . . . [a] tax is assessed not on unitary income but on discrete events such as sale, manufacture, and delivery, which can occur in a single State or in different States . . . [the] apportionment principle is not applicable; there is simply no unitary figure or event to apportion.

Tyler Pipe Industries, Inc. v. Washington State Department of Revenue, — U.S. —, 107 S. Ct. 2810, 2824-25 (1987) (Scalia, J., dissenting).

II. The Illinois Tax Discriminates against Interstate Commerce

A. The Equal Tax Rate Discriminates as It Places a Disproportionate Burden on Interstate Calls because of their Interstate Nature

In *Nippert v. Richmond*, the Court invalidated an annual license tax as discriminatory because, although applied equally to in-state and out-of-state solicitors, "the very nature of the market interstate operators serve prevents them from making full use of the privilege of doing business for which they have paid the state." 327 U.S. 416, 431 (1946) (fn. omitted); *accord*, *American Trucking Associations, Inc. v. Scheiner*, — U.S. —, 107 S. Ct. 2829, 2940-41, fn. 16, 20 and 21 (and cases cited therein) (1987). Likewise, here, the Court should take cognizance of the difference between the interstate and intrastate markets and tax bases. Specifically, the tax base on which the interstate tax is applied expands because interstate calls tend to cost more than intrastate calls, while Illinois' right over this base simultaneously shrinks because interstate calls involve proportionately less Illinois activity than intrastate calls do. For these two reasons, together *and* separately, the "equal" tax falls with disproportionate weight on the interstate calls *because* of their interstate nature. GTE Sprint Br. at 4, 49; *American Trucking*, 107 S. Ct. at 2841-42; *Halliburton Oil Well Cementing Co. v. Reily*, 373 U.S. 64, 70 (1963) (equal tax rate discriminatory because interstate tax base larger).

The State cavalierly dismisses both these arguments. As to cost, the State claims that in-state calls are occasionally longer and costlier than interstate calls. But the uncontested record below shows that long distance calls do tend to cost more. GTE Sprint Br. at 45-46. The operation of the tax, given this tendency, invalidates it. *American Trucking*, 107 S. Ct. at 2842 and 2844 ("the general average of instances" proves discrimination).

As to the disproportionately heavy taxation of interstate calls resulting from applying equal rates to services provided entirely and only partially in-state (Goldberg Br. at 31), the State asserts that, by considering *all* interstate phone calls, only half of which allegedly will be taxed by Illinois as the originating state (the other half by terminating states), the Illinois tax effectively taxes interstate calls at half the rate intrastate calls are taxed. State Br. at 28. This analysis is mystifying and wrong. First, it is wrong to assume that only half the Illinois originating/terminating calls will be "charged" to and therefore taxed by Illinois. *See* discussion *supra* at 3, 5-6. Second, it also is wrong to assume that no other states will tax the calls charged to Illinois, even if the charges for calls were split between originating/terminating states. Other states having contact with these calls could tax them on different phases of the calling activity (*e.g.*, on access charges) and produce disproportionate burdens on, and discrimination against, interstate calling. *See* GTE Sprint Br. at 33-46.

B. Other Existing Taxes Create Multiple Burdens and the State's Rejoinder that the Tax Will Not Overlap with Taxes on Calls Billed Elsewhere Is False and Fails To Address Numerous other Instances of Multiple Taxation

Currently existing and apportioned taxes on interstate phone calls create, together with the Illinois tax, actual multiple taxation. GTE Sprint Br. at 35-39. The State simply ignores a number of the taxes which overlap with the Illinois tax, including apportioned taxes on charges for access services (GTE Sprint Br. at 37), apportioned taxes on charges for private line services (Goldberg Br. at 29), or apportioned taxes on gross receipts from telecommunications (Goldberg Br. at 29). *See also* Hawaii tax at App. E and F hereto. Nor does the State address the complete failure of the Illinois tax under the hypothetical multiple burden analysis. GTE Sprint Br. at 34-35. Indeed, the Illinois tax fairly withers under the multiple burdens test.

The State's only rebuttal is its unsubstantiated nonrecord assertion that "the vast majority of [interstate] calls are charged and billed to the same number," but this assertion cannot validate the tax. First, even if true, this claim addresses only *one* instance of multiple taxation arising from other states' existing taxes on calls originating/terminating and billed/paid in those states. *See* discussion *supra* at 16; GTE Sprint Br. at 36-37. Second, it is clear calls *may* be billed in locations different from the Illinois "service address" charge location, so we know Illinois overlap with taxes on calls billed in other states is possible, despite the State's assertion. MCI Br. at 4, pp. 1-2 *supra*. Third, the tax cannot rely on the vicissitudes of external charging/billing behavior to transform it into a constitutional tax, in any event. *Tyler Pipe Industries, Inc. v. Washington State Department of Revenue*, — U.S. —, 107 S. Ct. 2810, 2819 (1987) (fortuitous non-discrimination inadequate to save a tax); discussion at p. 5 *supra*.[19]

C. *Moorman* Does Not Excuse the Type of Multiple Burdens Imposed by the Illinois Tax

The State, admitting that the tax does create actual multiple burdens, maintains that this Court, in *Moorman Manufacturing Co. v. Bair*, 437 U.S. 267 (1978), held that such burdens are excusable. The Court clearly did not do so. In *Moorman*, the tax at issue possessed an apportionment formula with external consistency. Thus, the only "excusable" multiple burdens created by the application of the tax were residual, arising from general state-to-state diversities in apportionment methodologies. As this

[19] As already shown, Sprint and other carriers do not charge to a service address location, nor need they do so; their billing locations are a matter of customer choice; and charging/billing practices are discretionary. *See* discussion *supra* at 2-3. It is therefore certain that the charge and bill locations will not necessarily coalesce, dooming the tax. *Cf. Armco, Inc. v. Hardesty*, 467 U.S. 638, 644-45 (1984) (constitutionality of tax cannot depend on shifting external events).

Court has clearly stated, that case has no application to the type of inherently unapportioned tax at issue here. *Japan Line, Ltd. v. County of Los Angeles*, 441 U.S. 434, 455 (1979).

D. The Internal Consistency Test Must Include an Analysis of the Application of Like Taxes and, Properly Applied, Condemns the Tax

The State claims that the Illinois tax possesses internal consistency since, if a tax *identical* to the Illinois tax were applied in every jurisdiction, there would be no multiple taxation. Yet, the test must include consideration of the application of the tax at issue together with the application of substantively equivalent taxes, precisely because this Court is not in the business of devising nationwide statutory schemes. For example, if the State's test were applied, the Illinois tax scheme might survive; however, other states' existing taxes on calls originating/terminating and billed there would have to be struck down, to eliminate the multiple taxation resulting from their overlap with the Illinois tax. But, in terms of the respective states' rights to tax such calls, there is no real distinction between these two taxing schemes which justifies preference of one over the other; the only difference is that Illinois taxes originating/terminating calls because charged in Illinois and the other states tax originating/terminating calls because billed there. As a consequence, applying the State's identical tax test would produce a completely arbitrary invalidation of taxes nearly indistinguishable from the Illinois tax, and would seriously hamper states' overall freedom in fashioning their taxing schemes. It must therefore be rejected. *See* GTE Sprint Br. at 26-29; *Western Live Stock v. Bureau of Revenue,* 303 U.S. 250, 256 (1938) (emphasis added) (vice characteristic of those [taxes] . . . held invalid is that they have placed on the commerce burdens of such a nature as to be capable, *in point of substance,* of being

imposed. . . or added to. . . with equal right by every state which the commerce touches. . .).[20]

E. The External Consistency Test Condemns the Tax and GTE Sprint's Proof Sufficiently Demonstrates It

The State claims that GTE Sprint has failed to prove that the tax fails the external consistency test because it has not submitted collective call information to show that "a highly disproportionate percentage of [all] calls between parties in Illinois and parties in other states are charged to service addresses in Illinois." State Br. at 32. GTE Sprint has already demonstrated -- through individual call examples, through the fallacies in the State's presumptions regarding charging "patterns," and through the admissions in MCI's *amicus* brief -- that the Illinois system has *no* ability, individually or collectively, to winnow out the economically significant Illinois activity or costs which contribute to interstate calling. The State's ploy of asking GTE Sprint to throw the fourth strike cannot save the tax. GTE Sprint Br. at 29-31; *see* discussion *supra* at 2-3, 5-7 and fn. 5 and 7.

III. The Illinois Tax Is Not Fairly Related to the Activities of the Taxpayer in the State

Although GTE Sprint has already shown otherwise, the State suggests that, as long as a taxpayer is somehow connected to activity taxed by Illinois, the measure of the tax must perforce be "fairly related" to the taxpayer's activities in Illinois. This test the State derives from *Commonwealth Edison Co. v. Montana,* 453 U.S. 609 (1981) where, unlike here, there was no problem relating the measure of the tax to the taxpayer's activities because *all* the taxpayer's activities occurred within the taxing state. State Br. at 34.

[20] *See also, Coverdale v. Arkansas-Louisiana Pipe Line Co.*, 303 U.S. 604, 613 (1938) (Commerce Clause issue is whether two taxes laid on same activity either in form or substance); *Southern Pacific Co. v. Gallagher,* 306 U.S. 167, 174 (1939) (where "*similar* levy . . . may be imposed . . . [on] the same taxable event").

The State nevertheless claims the Illinois tax fits the *Commonwealth* mold because, it asserts, at least one party, the taxpayer, is present in Illinois for the duration of the call, and because the call is charged to an Illinois "service address." Yet some calls will be taxed by Illinois when the taxpayer participant is *not* located in Illinois to make or receive the call. MCI Br. at 4. In addition, it is clear that, although one call participant may be at and charge a call to an Illinois address, that taxpayer must still rely on concomitant out-of-state transmission and origination/receipt activity to make/receive the call. The taxpayer may also pay for the call outside the state and the taxpayer can be billed by carriers or third party vendors located anywhere. *See* discussion *supra* at 2-3. Thus, unlike *Commonwealth*, a large percentage of the taxpayer's economically significant activity does or can take place outside Illinois. However, as already demonstrated, the Illinois tax is utterly incapable of even roughly adjusting itself to the varying amount of the taxpayer in-state activities, on either an individual or collective call basis, although, because of this variation, it should. GTE Sprint Br. at 29-31; *see* discussion *supra* at 5-6.

Respectfully submitted,

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August 5, 1988

APPENDICES

APPENDIX A

In the
SUPERIOR COURT
of the
DISTRICT OF COLUMBIA

U S SPRINT COMMUNICATIONS COMPANY, TMC LONG DISTANCE OF WASHINGTON, INC. STARNET INTERNATIONAL INC. *Plaintiffs,* CABLE & WIRELESS COMMUNICATIONS, INC., *et al.*, *Intervenors,* v. MARION S. BARRY, JR., HAROLD L. THOMAS, DISTRICT OF COLUMBIA, *Defendants.*	C.A. 8599-87 No. 4011-87 (Tax Division)
AMERICAN TELEPHONE & TELEGRAPH COMPANY AND AT&T COMMUNICATIONS OF WASHINGTON, D.C., INC. *Plaintiffs,* v. MARION S. BARRY, JR., HAROLD L. THOMAS, DISTRICT OF COLUMBIA, *Defendants.*	C.A. 10080-87

PLAINTIFF CARRIERS' PROPOSED FINDINGS OF FACT AND CONCLUSIONS OF LAW

* * * *

37. Most jurisdictions employ some sort of formula to apportion, for purposes of their gross receipts or similar tax, among the jurisdictions involved, the revenue from the long-distance or interstate telecommunications service which is subject to the tax and apply such a tax only to the portion of such revenue which is properly apportionable to activities within its borders. Usually, this apportionment is determined by reference to a ratio which compares the extent to which some index of measurement--such as wire mileage or value of personal property--is present in the taxing jurisdiction vs. the extent of the index generally. (Eggert testimony, Tr. 207-208).

38. In the absence of such apportionment, the same revenue from the same transaction can be subject to taxation by two or more states. This cannot happen if each state taxes only that revenue fairly apportionable to it. (Eggert testimony, Tr. 209-10; Many testimony, Tr. 258).

* * * *

43. The Act and regulations* do not apportion the revenues of each subject call between the District of Columbia and the other state or foreign country in which the call originated or terminated. The Act taxes subject calls on an "all or nothing" basis, *i.e.*, it taxes 100 percent of the price of each subject call. Built into the carrier's price for each call is the cost of access on the originating end, the cost of inter-LATA transmission, and the cost of access on the terminating end. By virtue of the interstate nature of the subject calls only one of the access costs is incurred within the District of Columbia, and only a small segment of the inter-LATA carriage. (Judicial notice; Eggert testimony, Tr. 207-08, 220; Many testimony, Tr. 270).

* * * *

* Gross Receipts Tax Amendment Act of 1987, Act 7-47, 34 D.C. Reg. 5068 (1987).

APPENDIX B

[Excerpts from GTE Northwest Incorporated's Practice Service Office System Series]

(Practice No. 052315003NW, Subsection 3)

3. BILL ADDRESS – DOMESTIC

3.01 A bill address is a customer-provided address, other than the service address, to which a bill is to be mailed. All domestic addresses conform to the standard format of city, state, and zip code.

3.02 The mnemonic BA= identifies the domestic bill address sentence.

3.03 The +BA= sentence normally contains the following elements and is written in accordance with the field parameters established for service address, with the exception of the bill post office phrase.[1]

a. House Number — five characters
b. Fraction — three characters
c. Street Direction — two characters
d. Street Name — 18 characters
e. Sublocation — 10 characters (SLOC=)
f. Billing Post Office (BPO=)

   1. City or Community — 13 characters
   2. State — two characters
   3. Zip Code — five characters (ZIP=)

* * *

(Practice No. 052315002NW, Subsection 23)

23. SERVICE ADDRESS

23.01 Service address designates the specific location of terminating telephone equipment. It is used to satisfy all address requirements in the system unless superseded by other address data written in another service order category. Its format is consistent with Listing Category coding requirements.[23]

23.02 The mnemonic SA= identifies a service address sentence. It is written with a plus (+) action indicator. A service address is required on I and T orders. It can be changed on C and R orders, but it can never be deleted. It is invalid on F and O orders.

23.03 Service address sentence may contain the following fields:

a. House Number and Fraction (optional)

b. Street Direction (optional)

c. Street Name (optional)

d. Sublocation (optional)

e. City or Community (optional)

f. Zip Code (optional)

* * *

APPENDIX C

[US Sprint Customer Order Form]

US Sprint

MIS SERVICE ORDER FORM

DIVISION ____ BRANCH ____ DATE SOLD ____ ACTV DATE ____ CUSTOMER ID # ____

SALES REP ____ S.S. # ____ SIC # ____

TYPE OF SERVICE: ☐ ANI ☐ DIALER ☐ DIAL-UP ☐ TRAVELCARD ONLY ☐ TBS

ADD ON TO: ☐ CIS ☐ CISB ☐ GTE ☐ UST EXISTING ACCOUNT # ____ EST VOLUME $ ____ PREVIOUS CARRIER ____

BILL TO: CUSTOMER ____ BILLING PHONE NO ( )

ADDRESS ____ SUITE ____

CITY ____ STATE ____ ZIP ____

PHYSICAL LOCATION: ADDRESS ____ SUITE ____ PHYSICAL PHONE NO ( )

CITY ____ STATE ____ ZIP ____

CONTACT #1 ____ TITLE ____ PHONE NO ( )

CONTACT #2 ____ TITLE ____ PHONE NO ( )

ANI ORDERS: EQUAL ACCESS CUT DATE ____ CHECK BOXES BELOW FOR ANIS WITH ACCOUNT CODE FEATURE (ACF)

CUSTOMER TELCO BTN ( ) LIST ALL EQUAL ACCESS LINE NUMBERS TO BE SUBSCRIBED.

IF CUSTOMER'S TELCO BTN SHOULD BE SUBSCRIBED, LIST IT HERE

(continued on the following page)

AUTO DIALER ORDERS: NO. LINES ______ ACCOUNT CODES ☐ YES ☐ NO NO SPEED PKGS. ______
☐ PBX ☐ EKS ☐ KEYSET ☐ POT ☐ TOUCH ☐ ROTARY SYSTEM FEATURES. ☐ SPEED CALL ☐ CALL FORWARD
NAME OF PHONE SYSTEM ______ MODEL NO. ______ INTERCONNECT CO. ______ PH. # (____) ______
LIST ALL LINE NO.'S TO BE COVERED WITH DIALERS:

(____) ______ (____) ______ (____) ______ (____) ______
(____) ______ (____) ______ (____) ______ (____) ______
(____) ______ (____) ______ (____) ______ (____) ______

NOTES ______

DIAL-UP SERVICE
NUMBER OF DIAL-UP CODES. ______
TRAVELCARD ONLY: NO. CODES ____ NO. CARDS ____
ACCOUNT CODES: CITY. STATE PHONE NO.
☐ YES ☐ NO ______ ______ (____) ______
☐ YES ☐ NO ______ ______ (____) ______

FEATURES: NO. TRAVEL CODES ____ NO. TRAVELCARDS ____ NO. INSPRINT PKGS ____ NO. SPEED DIAL PKGS ____ CALL DETAIL ____

BANK ______ BRANCH ______ CITY ______ STATE ______
TRADE REFERENCE #1 ______ CITY ______ STATE ______
CONTACT ______ PHONE NO. (____) ______
TRADE REFERENCE #2 ______ CITY ______ STATE ______
CONTACT ______ PHONE NO. (____) ______
TRADE REFERENCE #3 ______ CITY ______ STATE ______
CONTACT ______ PHONE NO. (____) ______

SALES REP ______ VERIFIED BY ______ MANAGER ______

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APPENDIX D

[Excerpts from US Sprint's Tariffs]

US SPRINT

TARIFF F.C.C. NO. 1
Original page ____
5th Revised page 50
Cancels 4th page 50

SPECIALIZED COMMON CARRIER SERVICE

5. RATES AND CHARGES

5.2 Usage Rates for Sprint Service From the Contiguous United States and Hawaii

A. Per-Minute Rates

This rate table should never be used without consideration of a subscriber's total usage and the application of usage discounts as described in Section 5.2.B. These rates also apply to calls made by Casual Callers.

Mileage	Day First	Day Add'l	Evening First	Evening Add'l	Night First	Night Add'l	
1-10	.1871 (R)	.1396 (R)	.1241	.0867	.0892	.0657	(C)
11-22	.2299	.1695	.1534	.1104 (R)	.1027	.0845	
23-55	.2349	.1895	.1649	.1234	.1044	.0939	
56-70	.2398	.2095	.1696	.1364	.1047	.1038	
71-124	.2410	.2095	.1696	.1364 (R)	.1047	.1038	
125-292	.2425	.2395	.1696	.1549	.1047	.1044	
293-430	.2525	.2495	.1699	.1624 (R)	.1058	.1054	
431-925	.2900	.2694	.1879 (R)	.1754	.1449	.1348 (R)	
926-1910	.3070	.2694	.2017	.1754	.1501	.1349	
1911-3000	.3227	.2794	.2211 (R)	.1819	.1640	.1399 (R)	
3001-4250	.3370	.3194	.2521	.2079	.1882	.1397	
4251+	.3530 (R)	.3394 (R)	.2649	.2209 (R)	.1967	.1691	(C)

B. Usage Discounts

As specified in the chart below, a subscriber will receive a discount on his monthly bill determined by his total monthly usage of Sprint Dial-1 and Dial-Up services. This discount will be applied to those calls between points within the contiguous United States and Hawaii and to Alaska, Puerto Rico, the U.S. Virgin Islands and Canada. To calculate the discount, the subscriber's relevant usage is multiplied by the appropriate percent discount shown below. Subscribers will receive the usage discount in effect at the close of each subscriber's billing period. Usage Discounts do not apply to Casual Callers or calls processed by using Credit Card Reader Phones.

Rate Period		Total Usage	
	$ 0-24.99	$25-99.99	$100+
Day Time	0.0%	3.0%	6.0%
Evening	0.0%	1.0%	2.0%
Night/Weekend	0.0%	1.0%	1.0%

ISSUED:	ISSUING OFFICER:	EFFECTIVE:
February 11, 1988	US Sprint Communications Co. Marybeth M. Banks 1850 M Street, N.W. Suite 1110 Washington, D.C. 20036	March 1, 1988

SPECIALIZED COMMON CARRIER SERVICE

4. SERVICE AND RATE DESCRIPTION (Continued)

4.4.A Sprint Advanced WATS, Sprint Advanced WATS Plus, Dial "1" WATS, Ultra WATS, US Sprint Direct 800 and US Sprint Ultra 800 Service Areas

The following matrix is to be used to determine the appropriate rate band. For SAW, SAW Plus, Dial "1" WATS and Ultra WATS, find the subscriber's NPA in the left hand column and follow the row across to identify the rate band below the terminating NPA. Then locate the corresponding per-minute rates for the appropriate WATS service as specified in Sections 5.1.B.1, 5.1.C.1, 5.1.D.1 and 5.1.E.1. For US Sprint Direct 800 and US Sprint Ultra 800, locate the subscriber's NPA in the left hand column, then follow the row across to identify the rate band below the caller's NPA. The corresponding rates will be found in Sections 5.1.H.1 and 5.1.I.1.

Subscriber's NPA	201	202	203	205	206	207	208	209	212	213	214	215	216
201		1	1	3 Z	5	1	5	5	1	5	4	1	2
202	1		2	3	5	3	5	5	1	5	4	1	2
203	1	2		4	5	1	5	5	1	5	4	1	3
205	3	3	4		5	4	4	4	3	4	3	3	3
206	5	5	5	5		5	2	3	5	4	4	5	5
207	1	3	1	4	5		5	5	1	5	4	2	3
208	5	5 Z	5	4	2 Z	5		3	5	3	4	5	4
209	5	5	5	4	3	5	3		5		4	5	5
212	1	1	1	3 Z	5	1	5	5		5	4	1	2
213	5	5	5	4	4	5	3		5		4	5	5
214	4	4	4	3	4	4	4	4	4	4		4	4
215	1	1	1	3 Z	5	2	5	5	1	5	4		2
216	2	2	3	3	5	3	4	5	2	5	4	2	
217	3	3	3	3	4	4	4	4	3	4	3	3	3
218	4	4	4	4	4	4	4	4	4	4	4 Z	4	3
219	3	3	3	3	4	3	4	4	3	4	3	3	1
301	1	1	1	3	5	3	5	5	1	5	4	1	2
302	1	1	1	3 Z	5	2	5	5	1	5	4	1	2
303	4	4	4	4	4	4	3	3	4	3	3	4	4
304	2	1	3	3	5	3	4	5	3	5	4	2	1
305	4	3	4	3 Z	5	4	5	5	4	5	4	4 Z	4 Z
307	4	4	4	4	4	4	3	3	4	3	3	4	4
308	4	4	4	3	4	4	4	4	4	4	3	4	3
309	3	3	3	3	4	4	4	4	3	4	3	3	2
312	3	3	3	3	4	3	4	4	3	4	3	3	2
313	3	2	3	3	5	3	4	5	3	5	4	3	1
314	3	3	4	2 Z	4	4	4	4	3	4	3	3	3
315	1	1	1	3 Z	5	2	5	5		5	4	1	2
316	4	4	4	3	4	4	4	4	4	4	2	4	3

ISSUED:

June 17, 1988

ISSUING OFFICER:

US Sprint Communications Co.
Marybeth M. Banks
1850 M Street, N.W.
Suite 1110
Washington, D.C. 20036

EFFECTIVE:

July 1, 1988

SPECIALIZED COMMON CARRIER SERVICE

5. RATES AND CHARGES (Continued)

5.1 Usage Rates For US Sprint WATS From the Contiguous United States, Alaska and Hawaii (Continued)

H. Per-Minute Rates For US Sprint Direct 800

.1 The following per-minute rates apply for calls originating in the NPAs specified in Section 4.4.A and terminating in cities listed in Section 3.21.F. (except for cities in Hawaii). See Section 4.4.A. for the corresponding rate bands.

DAY

BANDS	0 to 24.99 Hours	25 to 49.99 Hours	50 to 99.99 Hours	Over 100 Hours
1	$0.1557	$0.1549	$0.1534	$0.1326
2	$0.1642	$0.1632	$0.1616	$0.1609
3	$0.1686	$0.1677	$0.1661	$0.1652
4	$0.1772	$0.1766	$0.1747	$0.1739
5	$0.1814	$0.1806	$0.1786	$0.1777

EVENING

BANDS	0 to 24.99 Hours	25 to 49.99 Hours	50 to 99.99 Hours	Over 100 Hours
1	$0.1234	$0.1227	$0.1221	$0.1214
2	$0.1302	$0.1296	$0.1289	$0.1282
3	$0.1339	$0.1331	$0.1324	$0.1317
4	$0.1407	$0.1399	$0.1392	$0.1386
5	$0.1441	$0.1432	$0.1426	$0.1419

NIGHT/WEEKEND

BANDS	0 to 24.99 Hours	25 to 49.99 Hours	50 to 99.99 Hours	Over 100 Hours
1	$0.1031	$0.1031	$0.1031	$0.1031
2	$0.1086	$0.1086	$0.1086	$0.1086
3	$0.1114	$0.1114	$0.1114	$0.1114
4	$0.1169	$0.1169	$0.1169	$0.1169
5	$0.1202	$0.1202	$0.1202	$0.1202

ISSUED:	ISSUING OFFICER:	EFFECTIVE:
June 2, 1988	US Sprint Communications Co. Marybeth M. Banks 1850 M Street, N.W. Suite 1110 Washington, D.C. 20036	June 16, 1988

SPECIALIZED COMMON CARRIER SERVICE

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4. RATES AND CHARGES

4.1 Inter-City Channels

.1 Channels for Analog Transmission

Analog channels are full-duplex and offered at the following rates:

A. Long Haul Charges

MILEAGE/CKT.	RATE/MONTH/CIRCUIT
1-50	$ 54.15 + $2.16/mile for every mile
51-100	112.95 + .98/mile for every mile
101-350	144.50 + .54/mile for every mile
351-500	156.10 + .51/mile for every mile
501-1000	259.84 + .29/mile for every mile
1001-1500	273.54 + .27/mile for every mile
Over 1500	291.30 + .26/mile for every mile

B. Discounts

Discounts will apply to the monthly recurring charge per circuit, including Local Distribution Facilities charges where applicable. (N) *

1. A 5% discount will apply for customer who has 100 or more installed terrestrial channels, each over 100 miles in length. (N) *

.2 Voice Grade Multipoint Channels

Section 4.1.1 rates apply to any segment of a multipoint channel.

(N) * Issued in accordance with Special Permission No. 86-643 of the Federal Communications Commission to be effective on not less than five days' notice.

ISSUED August 27, 1986 US Sprint Communications Company Marybeth M. Banks 1850 M Street, N.W. #1110 Washington, D.C. 20036 EFFECTIVE September 1, 1986

APPENDIX E

Hawaii's General Excise Tax Law Chapter 237 [Excerpts]

* * * *

§ 237-13 Imposition of tax. There is hereby levied and shall be assessed and collected annually privilege taxes against persons on account of their business and other activities in the State measured by the application of rates against values of products, gross proceeds of sales, or gross income, whichever is specified, as follows:

* * * *

(6) Tax on service business. Upon every person engaging or continuing within the State in any service business or calling not otherwise specifically taxed under this chapter, there is likewise hereby levied and shall be assessed and collected a tax equal to four per cent of the gross income of any such business; provided that where any person engaging or continuing within the State in any service business or calling renders such services upon the order of or at the request of another taxpayer who is engaged in the service business and who, in fact, acts as or acts in the nature of an intermediary between the person rendering such services and the ultimate recipient of the benefits of such services, so much of the gross income as is received by the person rendering the services shall be subjected to the tax at the rate of one-half of one per cent and all of the gross income received by the intermediary from the principal shall be subjected to a tax at the rate of four per cent; and provided that where any person is engaged in the business of selling interstate or foreign common carrier telecommunication services within and without the State, the tax shall be imposed on that portion of gross income received by any such person from service which is originated or

terminated in this State and is charged to a telephone number, customer, or account in this State notwithstanding any other state law (except for the exemption under section 237-23(a)(2)) to the contrary. If, under the Constitution and laws of the United States, the entire gross income as determined under this paragraph of a business selling interstate or foreign common carrier telecommunication services cannot be included in the measure of the tax, such gross income shall be apportioned as provided in section 237-21; provided that the apportionment factor and formula shall be the same for all persons providing such services in the State.

* * * *

§ 237-21 Apportionment. If any person, other than persons liable to the tax on manufacturers as provided by section 237-13(1), is engaged in business both within and without the State or in selling goods for delivery outside the State, and if under the Constitution or laws of the United States or section 237-29.5 or 237-29.6 the entire gross income of such person cannot be included in the measure of this tax, there shall be apportioned to the State and included in the measure of the tax that portion of the gross income which is derived from activities within the State, to the extent that the apportionment is required by the Constitution or laws of the United States or section 237-29.5 or 237-29.6. In the case of a tax upon the production of property in the State the apportionment shall be determined as in the case of the tax on manufacturers. In other cases, if and to the extent that the apportionment cannot be accurately made by separate accounting methods, there shall be apportioned to the State and included in the measure of this tax that proportion of the total gross income, so requiring apportionment, which the cost of doing business within the State, applicable to the gross income, bears to the cost of doing business both within and without the State, applicable to the gross income. [L 1941, c 115, §1; RL 1945, §5457; RL 1955, §117-18; am L 1959, c 277, §2; HRS §237-21; am L 1987, c 239, §5]

APPENDIX F

DEPARTMENT OF TAXATION

[Excerpts from Proposed] Rule Amending Chapter 18-237, Hawaii Administrative Rules

June 21, 1988

SUMMARY

§ 18-237-13, Hawaii Administrative Rules, is amended by amending subsection (f) with a new paragraph (3).

1. § 18-237-13 is amended.

* * * *

Section 18-237-13, Hawaii Administrative Rules, is amended by amending subsection (f) to read as follows:

* * * *

(3) Telecommunication Services.

(A) Scope. Paragraph (3) is intended to provide uniform rules of administrative procedure to govern the taxation of the telecommunication industry pursuant to section 237-13(6), HRS, of the general excise tax law. Paragraph (3) shall not apply to gross income that is taxable under chapter 239, HRS, the public service company tax law.

(B) Definitions. As used in this paragraph, unless the context otherwise requires:

"Directly related to Hawaii" means geographically located within Hawaii or allocated to Hawaii according to generally accepted accounting principles and practices.

"Foreign common carrier" means any person operating under the legal jurisdiction of a country other than the United States which

provides transmission service to the public in general or to specified classes of the public.

"Gross income" means the gross receipts, as defined in section 237-3, HRS, of a long distance carrier.

"Interexchange carrier" means any person which provides transmission service between calling areas within a state.

"Interstate telecommunications" means all telecommunications that either originate or terminate outside of this State.

"Intrastate telecommunications" means all telecommunications that originate and terminate within this State.

"Long distance carrier" means any interexchange carrier or foreign common carrier which purchases, installs, rents, or leases a telephone system, telecommunication system, or telecommunications service for the interexchange or foreign common carrier's own use to provide the interexchange or foreign common carrier or other persons with telephonic interstate or international telecommunication service which is wholly or partially independent of any local exchange system or an intrastate or interstate interexchange network or which is a substitute for any dedicated facility by which an interexchange or foreign common carrier provides a telephonic communication path in the State.

"Telecommunication service" means the transmission, conveyance, routing, or reception of any electronic, electromagnetic interactive transmission, or any other kind of energy force variations of information in any

form, including but not limited to voice, image, data, or printed copy signal by means of wires, cables, radio waves, laser microwaves, satellites, fiber optics, any combination of these media, or any other method now in existence or that may be devised.

(C) Application. (i) Paragraph (3) shall apply to all long distance carriers conducting business, by providing telecommunication service, in the State.

(ii) The income of a long distance carrier that is subject to tax is that portion of gross income received by any long distance carrier from telecommunication service which is originated or terminated in this State and is charged to a telephone number, customer, or account in this State.

(iii) Apportionment. Under the Constitution and laws of the United States, the entire gross income as determined in clause (ii) cannot be included in the measure of tax; such gross income shall be apportioned by using the apportionment formula in subparagraph (E)(i).

(D) Apportionment factor. (i) The apportionment factor shall be as follows:

$$\frac{\mathrm{HCOP}}{\mathrm{NHOA} + \mathrm{NHTA} + \mathrm{HCOP} + \dfrac{(\mathrm{HBI})}{(\mathrm{NBI})} \times \mathrm{NCOP}}$$

HBI = Hawaii Billed Income originating or terminating in the State and charged to a telephone number, customer, or account in the State.

HCOP = Hawaii Cost of Operations includes those costs charged, under a long distance carrier's

normal method of accounting, to the following tax return and Federal Communication Commission-prescribed account titles or their equivalents, which are directly related to Hawaii.

—Cost of Operations
—Contributions
—Bad Debts
—Operating Expenses
—Hawaii Originating or Terminating Connection
—Expenses or Access Fees or Costs
—General and Administrative Expenses
—Advertising Expenses
—Leases
—Payroll
—Maintenance, including repair to:
  Cables
  Central Office Equipment
  Buildings and Grounds
  Maintenance of Transmission Power
  Other Maintenance Expenses
—Depreciation and Amortization Expenses
—Traffic Expenses
—Commercial Expenses other than advertising
—General Office Salaries and Expenses other than general and administrative expenses and payroll
—Insurance
—Accidents and Damages
—Operating Rents
—Relief and Pensions
—Operating Taxes
—Miscellaneous Deductions From Income

NBI=Nationwide Billed Income received from providing telecommunication service.

NCOP=Nationwide Cost of Operations includes the tax return and Federal Communication Commission-prescribed account titles or equivalents described by HCOP above. NCOP specifically excludes costs included in HCOP, NHOA, NHTA,

and connection expenses or access fees not included in HCOP, NHOA, or NHTA.

NHOA=Non-Hawaii Originating Access Cost relating to HBI, which may be

(1) The actual non-Hawaii originating access cost relating to a specific call resulting in Hawaii billed income; or

(2) A reasonable estimate derived by using the nationwide or Hawaii trunk average access cost per unit to originate calls multiplied by the number of calls terminating in Hawaii resulting in Hawaii billed income; or

(3) A reasonable estimate using the proportional relationship of the Hawaii trunk originating and terminating access costs to derive the non-Hawaii originating access costs as a proportion of the total Hawaii terminating access costs.

NHTA=Non-Hawaii Terminating Access Cost relating to HBI, which may be

(1) The actual non-Hawaii terminating access cost relating to a specific call resulting in Hawaii billed income; or

(2) A reasonable estimate derived by using the nationwide or Hawaii trunk average access cost per unit to terminate calls multiplied by the number of calls originating in Hawaii resulting in Hawaii billed income; or

(3) A reasonable estimate using the proportional relationship of the Hawaii trunk originating and terminating access costs to derive the non-Hawaii terminating access costs as a proportion of the total Hawaii originating access costs.

Example: ABC Long Distance does not have figures for access costs for specific phone calls and decides it can reasonably estimate its non-Hawaii access costs on a per unit basis as allowed by (2). For ABC Long Distance, the originating access cost is eighty cents ($.80) and the terminating access cost is one dollar ($1.00) through the local exchange in Hawaii or on a nationwide basis for each call. If ABC Long Distance customers place 200,000 outgoing calls and receive 100,000 incoming calls during the reporting period, the NHTA would be estimated to be (200,000 × $1.00) $200,000 and the NHOA as (100,000 × $.80) $80,000.

Example: XYZ Long Distance decides to make its estimate for non-Hawaii access costs on a proportional basis as allowed by (3). Assume the same cost relationship for Hawaii-located originating and terminating access costs exist for XYZ as in the above example. Therefore, if it costs $1.00 to terminate a call in Hawaii and $.80 to originate a call, the originating access cost is equivalent to eighty percent of the terminating access cost. If XYZ Long Distance incurs four million dollars ($4,000,000) in originating access costs and one million dollars ($1,000,000) in terminating access costs in Hawaii, then XYZ Long Distance's non-Hawaii terminating access costs may be calculated as follows:

$$\frac{\$4.0M}{.8} = \$5.0M$$

XYZ Long Distance's non-Hawaii originating access costs may be calculated as follows:

$$\$1.0M \times .8 = \$.8M \text{ or } \$800{,}000$$

(ii) The apportionment factor shall be multiplied by the gross income received or accrued by each long distance carrier from telecommunication service which is originated or terminated in this State and is charged to a telephone number, customer, or account in this State to determine the portion of gross income subject to tax.

(iii) The apportionment factor shall be uniformly applied to the gross income received or accrued from telecommunication service by all long distance carriers conducting business within and outside of the State.

(iv) The director may periodically review, evaluate, and adjust the apportionment factor to reflect any changes in the industry as necessary.

(E) Apportionment formula. (i) The apportionment formula shall be as follows:

$$\frac{HCOP}{NHOA+NHTA+HCOP+\frac{(HBI)}{(NBI)}\times NCOP} \times HBI = AHGI$$

AHGI = Apportioned Hawaii Gross Income received from providing telecommunication service in the State.

All other components are as described in subparagraph (D)(i).

Example: Aloha Communications, a local long distance carrier with no portion of its operations located out-of-Hawaii, provides long distance telephone service exclusively to customers in Hawaii. The billings total for all long distance telephone calls that originate or terminate in Hawaii and which are billed to a customer, number, or ac-

count in Hawaii is ten million dollars ($10,000,000). Aloha's nationwide billings total is also ten million dollars ($10,000,000) as all of its billings are made to Hawaii customers. The Hawaii cost of operations amount to seven million dollars ($7,000,000). The nationwide cost of operations, which excludes the Hawaii cost of operations, is zero. The non-Hawaii originating access costs related to the Hawaii-billed calls income is one-hundred-fifty thousand dollars ($150,000). The non-Hawaii terminating access costs relating to Hawaii-billed calls is one million five-hundred thousand dollars ($1,500,000).

The gross income received from telephone calls originating or terminating in Hawaii and billed to a customer, number, or account in Hawaii is apportioned as follows:

$$\frac{\$7M}{\$.15M+\$1.5M+\$7M+\dfrac{(\$10M)}{(\$10M)}\times 0} \times \$10M =$$

$8,092,485.55

The factor set out in subparagraph (D)(i), multiplied by the long distance carrier's Hawaii billed calls income of $10,000,000, equals the amount of gross income that is subject to tax, in this instance, $8,092,485.55.

Example: ABC Long Distance Company, an out-of-state long distance carrier that sells long distance telephone services to nationwide customers, has a branch office located in Hawaii which provides long distance telephone services in conjunction with its out-of-state offices. The amount of the Hawaii billed calls income is one hundred million dollars ($100,000,000). The Hawaii cost of operations is seventy million dollars ($70,000,000).

The nationwide billed income is eight billion dollars ($8,000,000,000). The nationwide cost of operations, excluding the Hawaii cost of operations, Hawaii-related originating and terminating access costs, and non-Hawaii-related access cost, is three billion dollars ($3,000,000,000). The non-Hawaii originating access cost relating to Hawaii billed calls income is one million five hundred thousand dollars ($1,500,000). The non-Hawaii terminating access cost relating to Hawaii billed calls income is fifteen million dollars ($15,000,000).

The gross income received from telephone calls originating or terminating in Hawaii and billed to a customer, number, or account in Hawaii is apportioned as follows:

$$\frac{\$70M}{\$1.5M+\$15M+\$70M+\dfrac{(\$100M)}{(\$8B)}\times \$3B} \times$$

$100,000,000 = $56,451,612.90

The factor set out in subparagraph (D)(i), multiplied by the long distance carrier's Hawaii billed calls income of $100,000,000, equals the amount of gross income that is subject to tax, in this instance, $56,451,612.90.

(ii) The apportionment formula shall be uniformly applied to the gross income received or accrued from telecommunication service by all long distance carriers conducting business within and outside of the State.

(iii) The director may periodically review, evaluate, and adjust the apportionment formula to reflect any changes in the industry as necessary.
[Eff. ____________] (Auth: sections 231-3(9), 237-8, HRS) (Imp: section 237-13(6), HRS)

* * *

Nos. 87-826, 87-1101

IN THE
Supreme Court of the United States
OCTOBER TERM, 1988

JEROME F. GOLDBERG AND ROBERT MCTIGUE,
Appellants,
v.
ROGER D. SWEET, DIRECTOR OF THE ILLINOIS DEPARTMENT OF REVENUE, *et al.*,
Appellees.

GTE SPRINT COMMUNICATIONS CORPORATION,
Appellant,
v.
ROGER D. SWEET, DIRECTOR OF THE ILLINOIS DEPARTMENT OF REVENUE, *et al.*,
Appellees.

On Appeal from the Supreme Court of Illinois

REPLY BRIEF FOR APPELLANTS GOLDBERG AND McTIGUE

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IN THE

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OCTOBER TERM, 1988

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On Appeal from the Supreme Court of Illinois

REPLY BRIEF FOR APPELLANTS GOLDBERG AND McTIGUE

ARGUMENT

1. Fair Apportionment

a. The linchpin of the State's fair apportionment argument is the proposition that taxing 100% of some interstate calls and 0% of others reflects a legislative apportionment formula.[1] But this "formula" is simply a

---

[1] In this reply, we cite the Consolidated Brief for Appellees as "State Br.," the Brief of Amicus Curiae MCI Telecommunications

recent invention of appellate counsel;[2] the decision to tax 100% of the calls here at issue was certainly *not* part of a *legislative* apportionment scheme. There is nothing anywhere in the statute, its legislative history, or the record indicating that the legislature chose to tax the whole of Illinois-charged calls and none of non-Illinois-charged calls in order fairly to apportion its tax. Rather, as the Supreme Court of Illinois expressly determined, the legislature found that "the ties to the State and benefits derived from the State" were "substantial" as to the Illinois-charged calls but "minimal" as to all others; accordingly, the legislature chose to tax the former but not

Corporation as "MCI Br.," and the Brief of Amici Curiae National Conference of State Legislatures, *et al.*, as "NC Br." In addition, we cite our own brief on the merits as "Goldberg Br."

[2] Thus, both in its own motion for summary judgment and in its opposition to plaintiffs' motion for summary judgment, the State took the position that the tax was "not in need of apportionment" because it was levied solely on a local event. State's Memorandum in Support of its Motion for Summary Judgment at 15. The State therefore contended that "apportionment is not an issue." State's Memorandum in Opposition to Plaintiffs' Motion for Summary Judgment at 6, 11, 14. Now, before this Court, the State contends not only that the legislature has in fact apportioned the tax but that a more finely-tuned apportionment would be impossible, and further that plaintiffs failed in their burden to prove at trial that the State's formula produces disproportionate results and that a call-by-call apportionment is feasible. While we believe this new argument can easily be rejected on its merits (see pp. 4-7, 11-15 below), we do not believe the Court should consider it. *See, e.g., Jenkins* v. *Anderson*, 447 U.S. 231, 234 n.1 (1980) (declining to address issue raised by respondent because "[o]rdinarily, we will not consider a claim that was not presented to the courts below"); *Washington* v. *Yakima Indian Nation*, 439 U.S. 463, 476 n.20 (1979) (prevailing party may "defend its judgment on any ground *properly raised below* whether or not that ground was relied upon, rejected, or even considered" below) (emphasis supplied); *United States* v. *New York Telephone Co.*, 326 U.S. 638, 651 n.18 (1946) ("whatever its merits," point not made by appellee until case reached Supreme Court will not be considered).

the latter.[3] The pertinent constitutional rule is that a State may tax *no more* than its fair share of interstate commerce; accordingly, a legislature may constitutionally choose *not* to tax a certain type of interstate commerce; but where it *does* tax, it must apportion. This the legislature has not done *at all* with regard to the tax it chose to impose.[4]

b. Even if the tax were in fact based on the "formula" now advanced by the State's lawyers, that formula would not meet the fair apportionment requirement. Indeed, on its face, that "formula" directly and palpably violates the fundamental tenets of a fairly apportioned tax. As the Court held in *Norfolk & Western Railway Co.* v. *Missouri State Tax Commission*, 390 U.S. 317, 325 (1968) (citation omitted), "[a] State will not be permitted, under the shelter of an imprecise allocation formula or by ignoring the peculiarities of a given enterprise, to 'project the taxing power of the state plainly beyond its borders.'" Yet that is precisely what Illinois has done. Ignoring the fact that a substantial part of every interstate communication is necessarily based on activities outside its borders, the State has elected to tax the whole of such activities whenever they happen to have been charged to an Illinois address. This the State may not do.[5]

[3] Appendix to Goldberg Jurisdictional Statement ("GA") 15a.

[4] The fact that the cited apportionment "formula" is an afterthought of counsel rather than a deliberate choice of the legislature is significant in that "the States have wide latitude in the selection of apportionment formulas * * *." *Moorman Mfg. Co.* v. *Bair*, 437 U.S. 267, 274 (1978). Here the State has not "select[ed]" an apportionment formula at all; appellate counsel has created it after the fact. That creation is not entitled to "wide latitude" from this Court; it is entitled to none.

[5] As this Court held in *Container Corp. of America* v. *Franchise Tax Bd.*, 463 U.S. 159, 169 (1983), "the factor or factors used in

c. The State and its amici argue that it is reasonable to assume that one-half of all interstate calls in which a State participates will be charged in that State and one-half in others; accordingly, they contend, by taxing 100% of the Illinois-charged calls and 0% of the other calls, the State receives the same revenue it would have received through an apportioned tax on *each* call. State Br. 17; MCI Br. 20. The State and MCI, however, never explain why it is reasonable to assume equality in the aggregate value of interstate calls charged to Illinois and those charged to other States; neither do they point to any legislative determinations or reliable data to support this assumption; and they certainly did not present any evidence on the issue at trial, where the State acknowledged that the tax is completely unapportioned. We would suggest that where, as here, a tax is completely unapportioned on its face, it is the *State's* burden to prove that in practice the tax is effectively apportioned (or, at the very least, to assert that proposition at trial so that plaintiffs have an opportunity to meet it).

We would also suggest that the assumption relied on by the State and MCI is not only counterintuitive, but is shown to be unsound by readily available public documents. The truth is—as information before the FCC demonstrates—that the individual States do *not* have approximately equal values of interstate calls charged in-state and out. Rather, as one might expect, in any given period virtually every State—Illinois included—is either a net originator or net terminator of interstate calls by a substantial amount.[6]

the apportionment formula must actually reflect a reasonable sense of how income is generated." Yet, even though a significant portion of the income from every Illinois-charged interstate call is by definition attributable to other States, Illinois taxes it all.

[6] *See* Schedule DMD-1, pp. 2, 4 in 1988 Access Filing Tariff Reference Package on file with the FCC Industry Analysis Branch. The data on this Schedule are taken from filings made annually by

More importantly, even if the State's unfounded, belatedly-introduced assumption were true, it would not render the tax fairly apportioned. The necessary predicate of the State's position is that so long as the State ultimately receives approximately the amount of revenue which a fairly apportioned tax would produce, it does not matter that some (even most) of the various interstate commerce transactions producing the revenues are overtaxed. This reflects a complete misunderstanding of the purpose of the fair apportionment requirement. It is *not* designed as a revenue-raising measure for the States; it is designed to protect interstate commerce. As held in *Japan Line, Ltd.* v. *County of Los Angeles*, 441 U.S. 434, 447-448 (1979), "[*i*]*n order to prevent multiple taxation of interstate commerce*, this Court has required that taxes be apportioned among taxing jurisdictions, so that *no instrumentality of commerce* is subjected to more than one tax on its full value" (emphasis supplied).[7] The

all interexchange common carriers. The Schedule reflects both the total traffic sensitive minutes of use as well as originating and terminating carrier common line minutes of use for all interexchange carriers from the third quarter of 1986 through the second quarter of 1987.

[7] Illinois' only response to the threat that other States may tax the same calls already taxed by Illinois is that "[t]he Constitution may permit [it], but it seems hard to believe that it requires it," particularly when, in the State's view, there may be instances where taxing a recipient of "unwanted long-distance calls" would be "unfair." State Br. 24. This response misses the point. No one is arguing that the Constitution *requires* other States to tax all calls which Illinois has already taxed in full; neither is it for the courts to decide the extent to which a recipient should be spared a tax on unwanted calls. All such judgments are for the pertinent State legislatures. The point that matters is that those State legislatures would be constitutionally entitled to tax their fair portion of calls which Illinois has already taxed in full. This threat of multiple taxation is sufficient in and of itself to condemn the tax. *See, e.g., Tyler Pipe Indus., Inc.* v. *Washington State Dep't of Revenue*, 107 S. Ct. 2810, 2817 (1987); *Armco Inc.* v. *Hardesty*, 467 U.S. 638, 644-645 (1984).

State and its amici apparently believe that *some* instrumentalities of commerce and *some* taxpayers participating in that commerce may be subjected to multiple taxation, so long as other instrumentalities and other taxpayers are subjected to a lesser tax or no tax at all. But commerce and taxpayers cannot lawfully be netted out in that fashion; robbing Peter to pay Paul does not satisfy the constitutional command. Interstate commerce necessarily occurs on a transaction-by-transaction basis, and it is therefore protected by the Constitution on that same basis.[8] As the Court recently explained in *American Trucking Ass'ns* v. *Scheiner*:

> The * * * tax cannot be vindicated * * * simply because it arguably benefits [one] class [of taxpayers] * * * more * * * than another class * * *. As one commentator has observed, "[i]mplementation of a rule of law that a tax is nondiscriminatory because other taxes of at least the same magnitude are imposed by the taxing State on other taxpayers engaging in different transactions would plunge the Court into the morass of weighing comparative tax burdens." * * * The [taxes at issue] must stand or fall on their own. [107 S. Ct. 2829, 2843 (1987) (citation omitted).[9]]

[8] We know of no case where the Court has validated a tax that was clearly unconstitutional as to one transaction or entity, on the ground that the State foreswore a constitutional tax on another transaction or entity. For example, the Court stated in *General Motors Corp.* v. *Washington*, 377 U.S. 436, 441 (1964), that "the question" posed by the fair apportionment requirement is "whether the State has executed its power in proper proportion to *the appellant's activities* within the State * * *" (emphasis supplied). Similarly, the Court declared in *Armco Inc.* v. *Hardesty*, 467 U.S. at 642, that "a State may not tax *a transaction or incident* more heavily when it crosses State lines than when it occurs entirely within the State" (emphasis supplied). The focus is on the particular "transaction or incident," not the net revenue raising effect of the tax.

[9] The commentator relied on by the Court in *Scheiner* is Professor Hellerstein in his *State Taxation* treatise. In the same passage of the treatise quoted by the Court, Professor Hellerstein concludes that "both in principle and on practical grounds," the validity of a tax "does not take into account other taxes on other transactions, but limits itself to the transactions at issue." J. Hellerstein, 1 *State Taxation: Corporate Income and Franchise Taxes* ¶ 4.12[5], p. 150 (1983).

So too here: irrespective of whether or how Illinois chooses to tax interstate calls charged outside Illinois, the State's tax on 100% of the value of all interstate calls charged in Illinois must meet the fair apportionment requirement on its own. As we have shown, it does not.

d. The State and its amici argue at length that the Illinois tax is functionally equivalent to certain State sales and gross receipts taxes upheld by this Court. State Br. 12-16; MCI Br. 9-15. But the taxes they cite are not at all like the present one. With regard to sales taxes, the State and amici rely on cases where this Court approved a tax either on the in-state purchase price of goods that had previously traveled interstate or on the in-state sales of a company that operates interstate.[10] The rationale of such cases and the substance of the taxes they approved have no bearing here. The tax in this case, as both the trial court and the Supreme Court of Illinois determined,[11] is levied on the entirety of every interstate call charged to an Illinois service address; by definition, therefore, the tax falls on the whole of an event which is occurring in at least two States *at once* (the originating and terminating States) and is taxable by both those States. The "practical effect" of such a tax is accordingly not like the sales taxes this Court has approved; *those* taxes, as the Court recently made clear, were upheld because they were laid on a "separate activity con-

[10] *See, e.g., Standard Pressed Steel Co.* v. *Dep't of Revenue*, 419 U.S. 560 (1975); *General Motors Corp.* v. *Washington*, *supra*; *McGoldrick* v. *Berwind-White Coal Mining Co.*, 309 U.S. 33 (1940).

[11] GA 9a, 20a, 21a, 22a, 24a.

ducted wholly within [a single State] that *no other state has jurisdiction to tax.*" *Tyler Pipe Industries, Inc.* v. *Washington State Department of Revenue,* 107 S. Ct. at 2822 (emphasis supplied). That is simply not true of the present tax.[12]

The gross receipts tax case relied on by the State and its amici—*Moorman Manufacturing Co.* v. *Bair, supra*— is also inapposite. There, the Court held that Iowa could constitutionally apportion its tax on the gross receipts of an interstate vendor of animal feed on the basis of the vendor's sales within Iowa. Even if a similarly-apportioned tax on an interstate communications *carrier* were valid,[13] it certainly does not follow that a sales-based "apportionment" falling on telephone *users* should

[12] As the trial court stated: "Illinois is attempting to tax the entire cost of an interstate act which takes place only partially in Illinois. This tax *by its own terms* is not fairly apportioned." GA 24a (emphasis supplied).

In continuing to insist that the present tax be treated as a sales tax on a wholly in-state activity (State Br. 10 n.3), the State not only ignores the substantive effect of the tax; it also refuses to acknowledge the determination of the Illinois State courts that the incidence of this tax is on the whole of interstate calls, necessarily including the portions occurring outside Illinois. That determination binds not only the State's appellate counsel, but this Court as well. *See Exxon Corp.* v. *Dep't of Revenue,* 447 U.S. 207, 226 n.9 (1980); *Complete Auto Transit, Inc.* v. *Brady,* 430 U.S. 274, 276 n.2 (1977); *Colonial Pipeline Co.* v. *Traigle,* 421 U.S. 100, 107-108 (1975); *United Air Lines, Inc.* v. *Mahin,* 410 U.S. 623, 628 n.5 (1973); *Aero Mayflower Transit Co.* v. *Bd. of R.R. Comm'rs,* 332 U.S. 495, 499-500 (1947).

[13] It is not at all clear that the Court would or should apply *Moorman* to a sales-based gross receipts tax on an interstate communications carrier. In *Moorman,* in-state sales of a vendor of tangible goods were held to be a fair measure of that vendor's taxable in-state activity. As discussed, however, sales of tangible goods occur wholly within a single State and may for that reason be deemed a fair measure of in-state activity. The same cannot be said of the "sales" of an interstate carrier whose activity is by definition occurring simultaneously in more than one State.

be upheld. Again, the economic substance of the two taxes is radically different. The rationale for upholding a sales-based gross receipts tax on a single interstate company is that the in-state sales fairly measure the company's in-state activities. When all the company's transactions are aggregated, that specific company will be fairly taxed on a state-by-state basis. The same rationale plainly does not apply when a sales-based "formula" falls on an individual telephone user within a given State; obviously, taxing such a user on the full value of the call does not fairly measure the in-state portion of that taxpayer's interstate activity; and just as obviously, the transactions of *individual taxpayer users* cannot be aggregated for Commerce Clause purposes the same way the transactions of a *single entity* can be aggregated. Accordingly, as earlier discussed, even if it were true that when all Illinois telephone users are combined their total interstate telephone tax balances out—because some are taxed at 100% and some are taxed at 0%—this could not validate the 100% tax on some users.[14]

[14] The State also claims that because plaintiffs did not prove the amount of their injury from the tax, their claim must fail. State Br. 32-33. We do not think this contention should be seriously treated. As both lower courts recognized, this tax on 100% of certain interstate commerce is unapportioned on its face. The tax is unquestionably substantially higher than it would be if apportioned, has extracted hundreds of millions of dollars from Illinois taxpayers, and subjects their calls to multiple taxation. It was certainly not plaintiffs' burden at trial, nor is it an appropriate inquiry here, to quantify the precise amount by which the Illinois tax unconstitutionally overcharges the commerce at issue. The only question before this Court is whether the statute as drawn is unconstitutional. If it is, the Court should strike it down, leaving the remedy to the lower courts. As the Court held in *Maryland* v. *Louisiana,* 451 U.S. 725, 759-760 (1981):

> It may be true that further hearings would be required to provide a precise determination of the extent of the discrimination [against interstate commerce], but this is an insufficient

e. The remaining apportionment case relied on by the State and its amici is the Court's recent decision in *D. H. Holmes Co.* v. *McNamara*, 108 S. Ct. 1619 (1988). *Holmes* reviewed the constitutionality of a Louisiana use tax on some mail-order catalogs distributed in-state but purchased out-of-state. In one provision, the statute expressly provided that "there shall be no duplication of the tax," and in another provision extended a credit against the use tax to any taxpayer paying a similar use or sales tax on the same property to another State. The Court found the tax fairly apportioned for two reasons: (1) the State "provides a credit against its use tax for sales taxes that have been paid in other States"; and (2) "Louisiana imposed its use tax only on the 82% of the catalogs distributed in-state; it did not attempt to tax that portion of the catalogs that went to out-of-state customers." 108 S. Ct. at 1623-24. This reasoning supports our position, not the State's. The inescapable and overriding defect in the present tax is that Illinois, unlike Louisiana, has not limited its tax to the portion of interstate commerce occurring "in-state" but has, instead, "attempt[ed] to tax that portion * * * that went to out-of-state customers." [15] It is therefore not fairly apportioned under the rationale of *Holmes*.

reason for not now declaring the Tax unconstitutional * * *. We need not know how unequal the Tax is before concluding that it unconstitutionally discriminates.

[15] Moreover, contrary to the State's position (State Br. 26), *Holmes* did *not* reject our view (Goldberg Br. 23-26) that a credit provision, to be effective, should prevent *all* duplicative tax on the commerce, including a tax levied on a different party in the other taxing State. *Holmes* did not even consider that issue. It is true that a credit in the Louisiana statute was specifically extended only to a single taxpayer who paid a tax in both States. But in the sales/use tax situation, that is the only circumstance in which such "duplication of the tax" *could* occur, *i.e.*, that the same taxpayer would pay a sales tax in one State and then be subjected to a use tax in a second State; accordingly, it is not surprising that neither this Court nor the Louisiana statute addressed the circumstance where a second party might be involved in the transaction.

In the case of an interstate telephone call, however, there are *by definition* two parties who could be taxed; accordingly, to prevent duplicative taxation on the commerce a credit must be provided whenever *either* party has paid a second tax. Yet the Illinois statute provides no such credit. Nothing in the language of *Holmes* precludes the need for such a credit. Indeed, that language suggests that the Court assumed that the credit applied in *any* circumstance where duplicative tax might arise: "[t]he Louisiana taxing scheme is fairly apportioned, for it provides a credit * * * for sales taxes that have been paid in other States." *Id.* at 1623. *Accord Tyler Pipe*, 107 S. Ct. at 2821 ("a credit * * * for manufacturing taxes paid other States would presumably cure the discrimination").

f. The last apportionment argument advanced by the State and its amici is based on certain factual assertions made by MCI for the first time in this litigation. MCI contends that "it is virtually impossible to devise an apportionment formula that fairly reflects the involvement of each State affected by every individual interstate telephone call." MCI Br. 16. It furthermore contends that it was plaintiffs' burden at trial "to prove that apportionment is practicable before they could demand that one be made." *Id.* at 19 n.12. It contends, finally, that this Court held in *Scheiner* that "unapportioned taxes 'may be perfectly valid when administrative difficulties make collection of more finely calibrated user charges impracticable * * *.'" MCI Br. 18 (citing 107 S. Ct. at 2847).[16] MCI's legal assertions regarding apportionment are flatly wrong, and its belated factual assertions, even if credited by the Court, do *not* show that no fair method exists to apportion taxes on interstate telephone calls.

This case was decided on cross-motions for summary judgment in the trial court. MCI was a party-defendant in that court and, as did appellant GTE, MCI counterclaimed *against* the State and alleged that:

[16] The State makes these same arguments and, like MCI, the State stakes those arguments on this Court's considering and accepting MCI's belated factual assertions. See State Br. 16-25.

> The Tax Act does not fairly apportion its tax to services supplied within the State of Illinois since it taxes the entire charge for calls transmitted in interstate commerce. As a consequence, the tax discriminates against interstate commerce, is not fairly related to the services provided by the State, and violates the Commerce Clause of the United States Constitution. [Answer and Verified Counterclaim of Defendant MCI Telecommunications Corporation ¶ 10 at 14.]

MCI did not participate further in the trial court or in the Illinois Supreme Court. GTE, on the other hand, did participate throughout in both those courts and, in support of its summary judgment motion in the trial court, adduced factual evidence (in the form of a sworn affidavit) indicating that GTE has the administrative capability to bill its customers for whatever taxes might be imposed by various States on their apportioned share of interstate calls participated in by that customer.[17] Neither the State nor MCI disputed GTE's claim; neither of them adduced *any* factual evidence on the summary judgment motions; and certainly neither of them made any contentions whatsoever that a call-by-call apportionment of taxes on interstate calls is impossible and therefore not constitutionally required. Rather, as has been explained, the State took the view that the tax did not need to be apportioned because it applied only to a "local" activity; and MCI, of course, asserted that the tax is *not* fairly apportioned and therefore is unconstitutional.

Now, however, both MCI and the State wish to reverse themselves; they ask the Court to accept their untimely contradictions of GTE's properly adduced trial evidence and to credit their broad factual contentions that apportioning taxes on interstate phone calls is "virtually impossible." We submit that this Court should not permit them to try their case for the first time here.[18]

[17] Affidavit of Richard N. Wiley ¶ 14 (reproduced in the appendix to GTE Jurisdictional Statement ("GTE App.") at 9a).

We also submit that MCI is wrong to assert that it is plaintiffs' burden to show not only that a tax is not fairly apportioned, but also that it is feasible to apportion it. We know of no precedent holding or even implying that such a showing is an element of proof in a Commerce Clause claim—and neither MCI nor the State cites any such precedent. Where, as here, a plaintiff shows a tax to be unapportioned on its face, the tax has necessarily already failed the constitutional test imposed by *Complete Auto*. A plaintiff need show no more.[19] If *the State*

[18] As is true under the Federal Rule governing summary judgment, the counterpart Illinois Rule (Code of Civ. Proc. § 2-1005) has been construed to require the nonmoving party to come forward *at trial* with factual evidence to support any claim it makes as to a material disputed fact, particularly where, as here, the movant has supported its claim by affidavit. See "Supplement to Historical and Practice Notes" to § 2-1005 at 23 (1988). The State and MCI did not act in accordance with this rule. In any event, this Court decides cases on the basis of the record properly before it, not on the basis of new factual materials never presented to or considered by the lower courts. *See, e.g., Wygant* v. *Jackson Bd. of Education*, 476 U.S. 267, 278 n.5 (1986) (Powell, J.).

[19] By the same token, and again contrary to the State's position, where a tax is unapportioned, a plaintiff certainly has no burden to prove that the unapportioned tax produces "grossly distorted results." State Br. 12. That might be true, as in *Moorman*, if a State had adopted an imprecise formula for apportionment which the Court nevertheless deemed fair. But this is not such a case. As the Court said in *Japan Line* in distinguishing *Moorman*:

> In *Moorman*, the problem arose, not from lack of apportionment, but from mathematical imprecision in apportionment formulae. * * * This case, by contrast, involves no mere mathematical imprecision in apportionment; it involves a situation where true apportionment does not exist and cannot be policed by this Court at all. [441 U.S. at 455.]

Precisely the same is true here. A tax on interstate commerce that is unapportioned fails *Complete Auto*; no further evidence of its unconstitutionality need be shown.

believed that apportionment is not possible for some reason, it could have *defended* on that ground at trial. But the State did not do so; again, it should not be permitted to raise that factually-based defense (and assert evidence thereon) for the first time before this Court.

Moreover, and perhaps most importantly, even if the Court were willing to entertain that defense and credit the factual claims now advanced by MCI, those claims do *not* show that Illinois has no practical method available for apportioning its tax on individual calls charged in Illinois. At most, MCI's claims reflect technological difficulty in determining the precise movement of each call *between* the originating and terminating States and in assessing the relative contribution made to that movement by the *intervening* States. *See* MCI Br. 2-3, 7-8, 16-17. Indeed, the essence of MCI's brief is that "MCI believes that it is literally impossible at the present time to meaningfully apportion the charge for a particular call *among the States through which that call was transmitted*, for there is no way to ascertain the identities of those States." *Id.* at 2 (emphasis supplied). Even if MCI's "belief" on this point were correct, it does not follow that *no* fair apportionment is possible. Indeed, one simple mechanism for accomplishing that apportionment is readily available and is suggested by MCI's own claims.[20]

If MCI is correct that the identities of the States participating in the intervening transmission of each call are unknowable, then obviously no intervening State could have nexus to tax the call. There would certainly be no nexus in the case of those calls which MCI says move by satellite "without passing through any State other than the States of origination * * * and termination." MCI Br. 2. And, according to the State, even in

[20] Other available methods for fairly apportioning the tax are described in GTE Sprint's Reply Brief.

the case of non-satellite calls, the "limited contact between the telecommunication and the intervening states makes it uncertain whether the intervening states would possess nexus to tax the call at all * * *." State Br. 19-20. If the State and MCI are right in these claims, it simply means that as to each such interstate call, only the originating and terminating States may constitutionally tax the call; and, even if no other method for apportioning the tax between those two States were available, obviously a 50% apportionment between them could be selected as a "rough approximation"[21] of their relative participation in the interstate commerce.[22] And, just as obviously, a 100% apportionment to Illinois cannot by *any* measure be deemed fair. Such an "apportionment" should not be approved by this Court.

2. Discrimination

Having devoted most of their briefs to the fair apportionment requirement, neither the State nor its amici give much attention to the nondiscrimination requirement of *Complete Auto.* What attention they do give is largely a repetition of their arguments concerning fair apportionment and, significantly, they fail even to address our contention that *Scheiner* is dispositive on the discrimination question.

[21] This Court has often indicated that a tax may be based on a "rough approximation" of a State's participation in interstate commerce, particularly where precise, finely-tuned calibrations are not available. *American Trucking Ass'ns* v. *Scheiner*, 107 S. Ct. at 2847 n.26 & cases cited therein. But contrary to MCI's claim, this Court has never held—and it certainly did not hold in *Scheiner*—that a totally unapportioned tax is permissible even where a "rough approximation" for a fair apportionment is available.

[22] Permitting the originating and terminating States together to tax the whole of the call is further supported by the well-known fact, documented in the National Conference amici brief, that the bulk of the charge for interstate calls is attributed to services at either end of the calls, not to the intervening transmission. NC Br. 8-9.

a. We showed in our initial brief that the inevitable "practical effect" of laying the same 5% tax on the gross charge for interstate and intrastate calls alike is to levy a higher effective charge on interstate calls for the same (or lesser) in-state activity. This result, we said, is "plainly discriminatory" under *Scheiner*.[23] The State and its amici do not deny that this discrimination is inherent in the statute. Instead, they say that even though the State may have assessed a higher effective tax for interstate calls charged in Illinois (say a Chicago to Gary call charged to Chicago), it must be assumed that someone, sometime will make a corresponding interstate call that will not be taxed by Illinois at all (say a Gary to Chicago call charged to Gary). State Br. 27-28. This, of course, is the same argument the State made regarding fair apportionment and it should be rejected for the same reason: the Constitution does not permit a State to discriminatorily tax *some* interstate commerce and *some* taxpayers participating in that commerce, on the ground that other commerce and other taxpayers are not assessed at all. *See Scheiner*, 107 S. Ct. at 2842-43.[24]

b. The State also seeks to defend its flat-rate tax on the basis of two other decisions of this Court—*Commonwealth Edison Co.* v. *Montana*, 453 U.S. 609 (1981) and *Container Corp., supra*. *Commonwealth Edison*, according to the State, prohibits discrimination *only* where it consists of a penalty levied on commerce for crossing State lines; hence, because there is "no evidence" that "the cost of a long-distance call * * * has anything to do with crossing State lines," charging a higher effective rate for interstate calls is permissible. State Br. 27-28. It is undeniable, however, that interstate phone calls charged in Illinois cross State lines. It is also undeniable that part of the tax received by Illinois for such calls is derived from activities across its State lines. It is therefore inescapable that, as was true in *Scheiner*, Illinois is charging a higher effective rate on the in-state component of *interstate* commerce than on the comparable in-state component of *intrastate* commerce.[25] Whether or not Illinois did this purposefully to discriminate against interstate commerce, the "free trade among the several States" which the Commerce Clause protects is damaged all the same. *Commonwealth Edison*, 453 U.S. at 618.[26]

[23] Goldberg Br. 30-33 (quoting *Scheiner*, 107 S. Ct. at 2841). We also explained that the more costly the call, the greater the discrimination. Goldberg Br. 32 n.27.

[24] For its part, the National Conference refuses to acknowledge that there is even *some* discrimination under the statute, even as to individual calls. Indeed, National Conference does not even mention *Scheiner*. Instead, it finds dispositive that the Court in *Holmes* deemed the Louisiana use tax to be nondiscriminatory and that the Court relied on the State's use-tax rate being "equal" to its sales-tax rate. NC Br. 18-19. Once again, this ignores the substantive distinctions among the taxes at issue. There is no difference in practical effect when the same mail-order catalogs are subjected to either a 5% use tax or a 5% sales tax. But if Illinois lays an "equal" 5% tax on both a $5.00 Chicago-Los Angeles and a $1.00 Chicago-Joliet call, it necessarily has not treated the calls "equally" in proportion to their in-state activity.

[25] It is furthermore well known, and was expressly established by GTE's affidavit at trial, that "[t]he basic charge for an interstate toll varies according to the distance between the place the call originates and the place it terminates, *increasing in price as the distance between these points increases*." Wiley Affidavit ¶ 12 (GTE App. at 9a). Accordingly, contrary to the State's claim, costs of calls do in fact respond to the crossing of State lines; and, necessarily, the more lines a given call crosses, the greater will be the cost, and the higher will be Illinois' tax.

[26] The State's reliance on *Container Corp.* is equally unpersuasive. Again, rather than deal with the "practical effect" test for discrimination described in *Scheiner*, the State seeks to apply a test it believes it can pass—the "internal/external" test of *Container Corp.* See State Br. 32-33. Even assuming that test were applicable, the State fails it. The "more difficult requirement" of that test requires that a State's tax be apportioned in such a way as to "actually reflect a reasonable sense of how income is generated." 463 U.S. at 169. Illinois' tax does not begin to do this. The tax on

c. The State's final argument with regard to discrimination addresses the risk of multiple taxation to which Illinois' interstate calls—but not its intrastate calls—are subject.[27] The State claims that multiple taxation is constitutionally permitted where a State appropriately apportions its tax under *Moorman*. State Br. 30. While a tax fairly apportioned in accordance with *Moorman* may well avoid an unconstitutional risk of multiple taxation, we have already shown that the Illinois tax is *not* fairly apportioned in accordance with *Moorman*—or in accordance with any other case—and is in fact discriminatory.

3. Fair Relation

The Illinois tax violates not only the fair apportionment and nondiscrimination requirements, but also the requirement that the tax's "measure" be related to "the taxpayers' presence or activities in [the] State." *Commonwealth Edison*, 453 U.S. at 629. In essence, the State's and amici's only response to this violation is to cite *Holmes* and to declare that the full value of interstate calls *is* an appropriate "measure" for the taxpayer's in-state activities. See State Br. 34-36; NC Br. 20-22. But this case is not like *Holmes*; there, as was also true in *Commonwealth Edison*, the *full value* of the taxed activity occurred *in-state*. Recognizing this distinction, the State contends:

Illinois-charged interstate calls is not apportioned *at all* between the in-state and out-of-state income generated by those calls. Accordingly, the tax by definition accomplishes precisely what *Container Corp.* forbids—it attributes telephone-call income to Illinois that is "'out of all appropriate proportion to the business transacted * * * in that State.'" *Id.* at 170 (quoting *Hans Rees' Sons, Inc.* v. *North Carolina*, 283 U.S. 123, 135 (1931)).

[27] As we explained in our initial brief, this Court's cases have identified two prohibited kinds of discrimination under the Commerce Clause—the kind that subjects interstate commerce to a higher effective rate for in-state services and the kind that subjects that commerce to multiple taxation to which intrastate commerce is not subject. See Goldberg Br. 30-33.

> Here, there is at least one party, the taxpayer, present in Illinois for the duration of the taxed call, and, * * * [the tax] is measured by what he is willing to pay for the call. Nothing could be more closely related to the taxpayer's activity in Illinois. The fourth prong of *Complete Auto* is thus satisfied. [State Br. 34-35.]

This analysis misconstrues the purpose of the fair-relation prong of *Complete Auto*. As the Court explained in *Commonwealth Edison*, the reason that the "measure" of the tax must be related to the taxpayer's in-state activities is to ensure that the tax will be "tied to the *earnings which the State * * * has made possible * * *.*" *Commonwealth Edison*, 453 U.S. at 626 (quoting *Wisconsin* v. *J.C. Penney Co.*, 311 U.S. 435, 446 (1940) (emphasis supplied)). The Court recently reaffirmed this proposition in *Scheiner*, indicating that the axle taxes in that case violated the fair-relation requirement because they did not "vary directly with miles traveled or with some other proxy for *value obtained from the State*." 107 S. Ct. at 2844 (emphasis supplied).[28]

[28] In its final refusal to analyze the substantive effect of this tax, the State argues that *Scheiner*'s application of the fair-relation requirement need not be followed here because the *Scheiner* tax was denominated a "user fee." According to the State, where a "user fee" is at issue "it may be appropriate to require that the measure of the tax bear some relationship to the services provided by the State, but the same requirement is neither needed nor imposed for general revenue taxes." State Br. 8. But *Complete Auto*'s requirements are not avoided by changing the name of the tax and nothing in this Court's cases indicates that the fair-relationship requirement is inapplicable to "general revenue taxes." Rather, this Court is committed to the view that its "duty" in a Commerce Clause case is to determine the "practical operation" of the tax under attack, "whatever its name may be." *Maryland* v. *Louisiana*, 451 U.S. at 756. (Moreover, if the way Illinois has categorized the tax were significant, the Court should be aware that the tax has been denominated, among other things, "a use tax, *i.e.*, use of a privilege." GA 8a.)

Here, the tax is not measured either by earnings Illinois has made possible or by value obtained from the State; rather, a substantial part of the earnings and value that Illinois taxes are necessarily derived out of State. Worse, the greater those out-of-state earnings and values, the higher the Illinois tax. Such a tax is not "fairly related" to the taxpayer's in-state activities or to the protection Illinois has extended to those activities. Indeed, it is inversely related to them.

CONCLUSION

For the foregoing reasons, and those stated in our initial brief, the judgment below should be reversed.

Respectfully submitted,

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Nos. 87-826, 87-1101

In the Supreme Court of the United States

OCTOBER TERM, 1988

JEROME F. GOLDBERG and ROBERT MCTIGUE, APPELLANTS

v.

ROGER D. SWEET, DIRECTOR OF THE ILLINOIS DEPARTMENT OF REVENUE, ET AL., APPELLEES.

GTE SPRINT COMMUNICATIONS CORPORATION, APPELLANT

v.

ROGER D. SWEET, DIRECTOR OF THE ILLINOIS DEPARTMENT OF REVENUE, ET AL., APPELLEES.

On Appeal from the Supreme Court of Illinois

SUPPLEMENTAL BRIEF OF APPELLEES PURSUANT TO RULE 35.5

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16 pp

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On Appeal from the Supreme Court of Illinois

SUPPLEMENTAL BRIEF OF APPELLEES PURSUANT TO RULE 35.5

Appellees Roger D. Sweet, Director of the Illinois Department of Revenue, *et al.*, through their undersigned counsel, respectfully submit this supplemental brief pursuant to Rule 35.5 of the Rules of this Court. The purpose of this brief is to call the Court's attention to a letter dated October 7, 1988, from counsel for the State of Hawaii to counsel for all parties in these consolidated cases. The letter, which is self-explanatory, responds to certain statements regarding Hawaii's tax on interstate telecommunications made in the reply brief of ap-

pellant GTE Sprint in No. 87-1101. It is attached hereto. The subject matter covered in the attached material only recently came to appellees' attention and constitutes intervening matter not available at the time of filing of appellees' brief on the merits. It is therefore a proper subject for a supplemental brief under Rule 35.5.

Respectfully submitted.

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APPENDIX

APPENDIX

[SEAL]

STATE OF HAWAII

DEPARTMENT OF THE ATTORNEY GENERAL
TAX DIVISION

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October 7, 1988

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Re: *Goldberg and GTE Sprint v. Sweet*, Nos. 87-826, 87-1101

Dear Sirs and Madam,

It has come to our attention that the Reply Brief of Appellant GTE Sprint Communications Corporation in

this case filed on August 5, 1988, contains certain incomplete and misleading references to the Hawaiian tax on interstate telecommunications.

On pages 10-12 of its Reply Brief in a section on supposed "realistic alternatives" to the Illinois Tax, GTE Sprint implies that Hawaii has selected a cost-based apportionment formula for each carrier as an alternative to the Illinois system. GTE Sprint suggests that the experience in Hawaii and other states "proves that the actual assessment of taxes, using such alternative formulas, will pose no administrative burden," and that Hawaii's "more sensitive" formula is "superior" to the Illinois method because the Illinois approach is "arbitrary" as compared to those like Hawaii which utilize "economically substantive *indicia*" of instate contributions to interstate calling. Id. at p.12.

The actual situation in Hawaii is substantially different:

1. Hawaii did not choose, and does not want, the complex cost-based carrier-by-carrier apportionment system. In fact, it chose a system virtually identical to Illinois' system, taxing all calls to and from Hawaii charged to a person in Hawaii. Under the Hawaiian statute a backup provision for specific carrier-by-carrier cost-based apportionment is triggered *only if* "under the Constitution and Laws of the United States" the entire amount otherwise taxed cannot lawfully be taxed. See Hawaii Rev. Stat. § 237-13(6); GTE Reply, Appendix E at E-2.

2. Rather than finding the Hawaii alternative "realistic" or of "no administrative burden," in May GTE Sprint's successor, U.S. Sprint, through the same attorney as appears in this case (Mr. Wiley) and later through another attorney (on the very same date as the Reply Brief), *objected* to the proposed Hawaiian apportionment regulations cited in the brief. They contended that the apportionment system lacked "certainty," depended on "accounting judgments," would "result in greater confusion for our customers and potential difficulty for our company to fully collect the tax," (Wiley letter to Hawaii Director of Taxation, May 20, 1988, attached as Ex. A, at p. 3.), would cause "administrative problems" arising from the "judgment calls and estimates [which] . . . may not accurately reflect the actual costs" and "additional administrative burdens due to the changing costs," and would "contribute to customer confusion," burdens which would trouble both Sprint and the state. (Sprint Testimony before State Department of Taxation, August 5, 1988, attached as Ex. B, at pp. 2-3).

3. Contrary to its position in the Supreme Court criticizing "arbitrary" formulas and preferring "more sensitive" formulas like the fallback option proposed in Hawaii, in fact, in its Hawaii filings, Sprint objected to the actual results of the formula precisely because its sensitivity produced a different apportionment factor for each interstate carrier based on its unique cost structure. Rather Sprint strongly pushed for a single, arbitrarily determined apportionment factor for all the competing companies regardless of their different actual levels of activity in Hawaii, totally eliminating the sensitivity in the original formula because the differences might "disadvantage" some companies and "confuse" customers. Testimony at p. 2. (The single figure suggested was 33.6%).

In short, Hawaii hopes, for many of the same reasons proffered by Sprint in Hawaii, that it will be able to implement fully its Illinois-type tax without having to revert to the complex and prolix rule promulgated as a backup in case the Supreme Court does rule against the equitable and straightforward Illinois system. It is

enough to read the regulation (printed in Appendix F to Sprint's Reply Brief) to understand why this is so. In any event, since Hawaii's rule cannot go into effect until January 1, 1989, that rule is not "experience in other states" supporting such a rule as "superior" to the Illinois approach. The only experience we have had thus far is that Sprint and others say the system is too cumbersome, too burdensome, too confusing, and too sensitive to differences among competitors.

We hope that the counsel arguing the case may have the opportunity to correct the record.

Very truly yours,

/s/ Kevin T. Wakayama
KEVIN T. WAKAYAMA
Supervising Deputy Attorney General
Tax Division

KTW:cm

EXHIBIT A

May 20, 1988

Richard F. Kahle, Jr.
Director of Taxation
State of Hawaii
Department of Taxation
P.O. Box 259
Honolulu, Hawaii 96809

Re: Draft of General Excise Tax Rules on Telecommunication Services

Dear Mr. Kahle:

Thank you for providing US Sprint with the opportunity to comment on the May 10, 1988 draft of the proposed rules for implementing the general excise tax on telecommunications, imposed at Section 237-13(6), Hawaii Revised Statutes, as enacted by H.B. No. 1764-86.

The proposed rule seriously conflicts with the language contained in H.B. No. 1764-86, and with the legislature's intent in passing the legislation. Specifically, the rule seems to violate the intent of the law in the following three areas: 1. It fails to clarify whether the entire gross income from taxable services will be subject to tax; 2. It provides for the use of different apportionment percentages for different carriers if the entire gross income is not subject to tax; and, 3. It uses apportionment criteria which are subject to considerable uncertainty.

With respect to the question whether the entire gross income will be taxed, the draft rule merely restates the language of Section 237-13(6), by providing that "[i]f, under the Constitution and laws of the United States, the entire gross income [received from service which is originated or terminated in this State and is charged to a

telephone number, customer, or account in this State] cannot be included in the measure of tax, such gross income shall be apportioned. . . ." Draft of amended Section 18-237-13(f)(3)(C)(iii) of the Hawaii Administrative Rules. The Department's proposal would essentially leave the long-distance carriers to guess whether or not the tax on their "entire gross income" is required to be reported on their tax returns, and collected from their customers.

The legislation clearly states that "the department of taxation *shall* have determined the amount properly apportioned to the State under Section 237-13(6)", *before* the tax may become effective. *See*, Section 3 of H.B. No. 1764-86 (emphasis added). Further, the Conference Committee Report (No. 68-86, April 18, 1986) stated "[s]ince the general excise tax is a separately stated tax which is customarily passed on to consumers, the Committee concluded that it was appropriate to commence collecting the tax upon the effective date of the Act and not to seek taxes for the period prior to that date." Thus, the legislature intended that the telecommunications carriers know in advance how the tax would be imposed, so that the customary practice of recovering the tax from customers at the time of billing could be accomplished. The proposed rule defeats this legislative intent due to its silence on the fundamental question of whether apportionment will be allowed. We recommend the rule be revised to state whether the tax will apply to the entire gross income.

The rule also diverges from the legal requirement that the apportionment *factor* not differ from carrier to carrier. Section 237-13(6) provides that "*the apportionment factor* and formula *shall be the same* for all persons providing [interstate and foreign telecommunication] services in the State." The Committee on Conference explained that this provision was necessary because "to the extent that different formulas are used, some

companies may be disadvantaged as compared to other companies and customers will be confused by billings at different effective tax rates." Conf. Comm. Rep. No. 68-86, April 18, 1986, at p. 2 (emphasis added). Further, the Committee noted that the aforementioned language had been "modified to clarify its intent that the 'apportionment factor and formula' and not the 'apportionment' of the gross income *shall be the same for all persons providing such service in the State.*" Conf. Com. Rep. at p. 2. Clearly, the legislature was attempting to insure that phone calls would be taxed under the new law at the same *effective* rate, regardless of the carrier used, in order to avoid giving a competitive advantage to companies with comparatively less activity in the State, and to avoid the customer confusion that would result if telecommunications carriers were charging different rates for the tax. For example, a $20 call from Honolulu to New York using Company X might carry a tax of 40 cents ($20 x 50% apportionment factor x 4% tax rate), while the same call using Company Y might bear a tax of only 20 cents (if Company Y's apportionment factor is 25%). We suggest that, in order to conform with the statute, the Department must devise an apportionment formula on an industrywide basis such that the resulting apportionment *factor*, may be applied *equally* to each carrier's gross income.

Finally, the proposed apportionment formula fails to provide telecommunications carriers with any certainty as to what their tax will ultimately be if the Department rules that apportionment is required. For example, the rule requires taxpayers to make accounting judgments in determining the costs of operations directly related to Hawaii, such as the Hawaii proportions of national advertising campaign expenses, national insurance coverage costs, etc. These judgments may be questioned on audit. As a result, taxpayers such as US Sprint will be uncertain as to what the tax will be, and what tax should

be billed to our customers. This will result in greater confusion for our customers and potential difficulty for our company to fully collect the tax.

In summary, the intent of the legislature and the final bill which was passed and subsequently signed by the Governor, envisioned the development by the Department of a single apportionment factor, based upon industry data, which would apply an identical effective tax rate to each carrier, so that no competitive effects or customer confusion would result from the tax. The draft rule does not accomplish this, and we respectfully urge the Department to adopt a rule conforming to the legislative mandate.

We would be happy to provide further comments or respond to any questions you may have.

Very truly yours,

/s/ Richard N. Wiley
RICHARD N. WILEY

/s/ Craig Smith
CRAIG SMITH
Attorneys for US Sprint

EXHIBIT B

U.S. SPRINT COMMUNICATIONS COMPANY

Testimony Before
The State Department of Taxation

August 5, 1988

U.S. Sprint Communications appreciates the opportunity to present comments on the June 21, 1988 draft of the Department of Taxation's proposed rules for implementing the general excise tax on communications. We appreciate the Department's desire to impose the tax in a timely and legally correct fashion and we are anxious to have the apportionment formula resolved in a manner that is both equitable and fair to the industry as well as to the State. However, U.S. Sprint believes the proposed rule has some shortcomings that threaten its equity, neutrality and administrative ease.

The proposed rule fails to comply with the requirement that the apportionment factor not differ from carrier to carrier. Section 237-13(6) provides that "the apportionment factor and formula shall be the same for all persons providing [interstate and foreign telecommunication] services in the State." The Conference Committee Report (No. 68-86, April 18, 1986) explained that this provision is necessary because "to the extent that different formulas are used, some companies may be disadvantaged as compared to other companies and customers will be confused by billings at different effective rates."

The tax is not equitable since it taxes at different effective rates similarly situated taxpayers providing the same services. Failure to provide the same effective rate for all companies and their customers produces a tax that is neither equitable nor neutral.

Further, certain administrative problems will occur for the Department as well as telecommunication com-

panies as a result of the proposed rules. The proposed apportionment formula fails to provide carriers with any certainty as to what their tax will be. The rules require accounting judgments to be made in determining the costs of operations directly related to Hawaii. For example, expenses such as the Hawaii proportions of national advertising campaign expenses and national insurance coverage costs suggest we make estimates. These judgment calls and estimates may be factually incorrect, and may not accurately reflect the actual costs. This process of guessing actual costs will make any audit process more difficult for the Department. As a result taxpayers will be uncertain and confused as to what the tax will be, and what tax should be billed to customers.

Additional administrative burdens exist due to the changing costs of Hawaii and non-Hawaii costs of operations. This proposed rule does not explain whether the companies should compute the factor each month when the returns are due or on an annual basis. If computed on a monthly basis, the changing effective rate will further inhibit companies' ability to accurately pass on the tax, and will further contribute to customer confusion.

These administrative burdens will not only prove difficult for U.S. Sprint and other telecommunication service providers, but also for the State, since the State would have difficulty in projecting future revenues.

Finally, we understand the Department has suggested the industry place a notice on customers' bills which states that the tax complies with Hawaii's 4% general excise tax. We realize this was suggested as a means to resolving some of the industry's concerns about marketing problems and the anti-competitive issues which result from an apportionment formula which is different for each carrier. Unfortunately this will not alleviate our concerns and will only lead to great customer confusion. The apportioned rate would remain unequal for companies, and many customers will notice upon calcula-

tion the differential rates. We believe this problem may be corrected with a minor adjustment to the Department's proposed regulations. This adjustment will be offered as a suggested amendment at the August 5th hearing.

Again, I think you for the opportunity to present U.S. Sprint's concerns. U.S. Sprint stands ready to provide further information to the Department or provide any other assistance requested to aid in the timely development of a fair and equitable apportionment formula.

HAWAII TELECOMMUNICATIONS TAX

Company	Hawaii Costs Related to Hawaii Income / Total Company Costs (Including Hawaii Costs Related to Hawaii Income)	= A Factor x	Hawaii Gross Income Originating or Terminating and Billed to Hawaii	= Hawaii Apportioned Income
Interstate	Per Regulation	40%	$ 15,000,000	$ 6,000,000
Global	Per Regulation	30%	$ 80,000,000	$24,000,000
Multistate	Per Regulation	20%	$ 10,000,000	$ 2,000,000
Instate	Per Regulation	50%	$ 20,000,000	$10,000,000
			$125,000,000	$42,000,000

Composite Weighted Average
($42M/$125M) 33.60%

—The use of a composite weighted average will eliminate marketing pricing differentials, competitive inequities and customer confusion.

—It supports a cost-based allocation mandated by the Hawaii statutes and supported by the Tax Department.

HAWAII TELECOMMUNICATIONS TAX

Company	Hawaii Billed Calls	Apportionment	Apportioned Income	Tax Rate	Tax
		DEPARTMENT METHODOLOGY			
Interstate	$15,000,000	40%	$ 6,000,000	4%	$ 240,000
Global	$80,000,000	30%	$24,000,000	4%	$ 960,000
Multistate	$10,000,000	20%	$ 2,000,000	4%	$ 80,000
Instate	$20,000,000	50%	$10,000,000	4%	$ 400,000
					$1,680,000
		DEPARTMENT METHODOLOGY/WEIGHTED FORMULA			
Interstate	$15,000,000	33.6%	$ 5,040,000	4%	$ 201,600
Global	$80,000,000	33.6%	$26,880,000	4%	$1,075,200
Multistate	$10,000,000	33.6%	$ 3,360,000	4%	$ 134,400
Instate	$20,000,000	33.6%	$ 6,720,000	4%	$ 268,800
					$1,680,000

Nos. 87-826, 87-1101

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GTE SPRINT COMMUNICATIONS CORPORATION,
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Appellees.

On Appeal from the Supreme Court of Illinois

BRIEF OF THE NATIONAL TAXPAYERS UNION AS AMICUS CURIAE IN SUPPORT OF APPELLANTS

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On Appeal from the Supreme Court of Illinois

BRIEF OF THE NATIONAL TAXPAYERS UNION AS AMICUS CURIAE IN SUPPORT OF APPELLANTS

Having obtained the written consent of the parties pursuant to Rule 36.2 of the rules of this Court,[1] the National Taxpayers Union submits this brief as amicus curiae, on behalf of the thousands of individual taxpayers who are its members, and respectfully suggests that this court should reverse the decision below.

[1] Copies of the consent letters have been filed with the Clerk.

INTEREST OF THE NATIONAL TAXPAYERS UNION

The National Taxpayers Union (hereinafter "NTU") is a nonprofit, membership organization devoted to protecting the interests of federal, state and local individual taxpayers through public education, lobbying and litigation on tax and spending issues. NTU's nearly 150,000 members have a direct economic interest in this action. First, as Illinois citizens and taxpayers, many NTU members are directly and adversely affected by the Illinois telephone tax. Second, if this Court upholds the decision of the Supreme Court of Illinois, NTU members throughout the United States may soon be subjected to similar taxes in their own jurisdictions.[2]

STATEMENT OF THE CASE

The Illinois Telecommunications Excise Tax Act, Ill. Rev. Stat. ch. 120, para. 2001-2021, imposes a tax (the "telephone tax") "upon the act or privilege of originating in this State or receiving in this State" interstate and intrastate telecommunications. Secs. 2002-2004. The tax is imposed at the rate of 5% of the "gross charge" for telecommunications purchased at retail in Illinois and billed to an Illinois address. *Id.* "Gross charge" is defined as "the amount paid for the act or privilege of originating or receiving telecommunications in this State and for all services . . . provided therewith . . .", excluding, *inter alia*, charges for customer equipment when such charges are "separately identified from other charges." Sec. 2002(a).

The tax reaches both "intrastate" and "interstate" telecommunications. Secs. 2003-2004. The statute defines "interstate telecommunications" as "all telecommunications that either originate or terminate outside this State."

[2] Numerous states, and even municipalities, now tax interstate telecommunications, as noted in the opinion below, and in the Goldberg Jurisdictional Statement (at 25 n.20 & 27 n.24).

Sec. 2002(d). Thus, the Act taxes long distance charges for both domestic and overseas calls. A credit is provided under sec. 2004 of the statute against any tax due from a taxpayer who has paid two or more taxes on the same interstate communication, but the taxpayer must provide specific "proof" of his or her eligibility for the credit, including apparently proof that the tax paid to the other state was "properly due." *Id.*

From the consumer's perspective, the tax is imposed on three items: the basic monthly charge for telephone service; any long distance charges; and any message unit charges incurred for local calls beyond those which are provided as a part of basic service. The economic effect of the tax differs in each case.

The basic service charge is a payment made for the right to access the telephone network. In the telecommunications industry, it is frequently referred to as a charge for "dial tone." In Illinois, as in much of the nation, one can purchase several types of basic service. These range from "unlimited" local service, which includes the right to make an unlimited number of free calls within a local calling area; to various budget plans, under which the consumer is entitled to a fixed number of local calls, with additional calls being subject to a small message unit charge; to "measured zero" service, under which the customer incurs a message unit charge on every local call.[3] Even in places which do not offer unlimited free calling throughout the local calling area, local calls within a fixed geographic radius of the caller's telephone typically carry only one message unit, regardless of duration.[4]

[3] Not all areas have all three types of plan. For example, residential subscribers in Peoria have a choice between "measured zero" and unlimited service within their local calling area.

[4] In the Chicago area, for example, this local radius is about eight miles.

Under any of these plans, the charge for basic telephone service is a fixed monthly charge, and the percentage tax imposed on it has a character of a "lump sum" tax. For example, a consumer with "unlimited" local service may make no local calls in a given month, or a thousand local calls. In either event, he pays the same amount of tax. His tax rate, at the margin, is zero. Thus while the tax may cause some low income consumers to forego telephone service entirely, it will have no effect at all on the local calling patterns of consumers who retain unlimited service. Nor, so long as they remain below their monthly allowance, will it have any effect on the local calling patterns of individuals with "budget" type services.[5]

On the long distance portion of the bill, the consumer is charged for using the long distance network. Charges vary as a function of the number of calls made, the locations called, their duration, and the time of day. Thus, as applied to long distance calls, the telephone tax is a true excise tax, in that it systematically increases the price of the item taxed by a fixed percentage. In so doing, it necessarily reduces consumption of that item—in this case, long distance services.

As applied to message unit charges, the telephone tax shows aspects of both a lump sum and an excise tax. It is a lump sum tax to the extent that it frequently does not vary with the duration of the call, or the location called.[6] It is an excise tax because it does vary with the number of calls made each month by an individual consumer over and above his basic allotment. Moreover, the amount involved per call (five cents per message unit in

[5] For a more extended discussion of the differences between lump sum taxes and true excise taxes in their effect on consumer behavior, see Koch, *Microeconomic Theory and Application*, 238-239 (Little, Brown & Co. 1976).

[6] This is the case, for example, for calls made in the Chicago area to points within approximately an eight mile radius of the caller's telephone.

Chicago for example) is typically very small by comparison with long distance charges for calls of the same duration.

Most intrastate telephone calls in Illinois are local, and many, if not most, local phone calls carry either a single message unit or no message unit charge. On the other hand, nearly all interstate calls from and to Illinois are long distance.[7] In these circumstances, a tax imposed as a flat percentage of all local and long distance telephone charges will systematically raise the marginal cost of making interstate telephone calls without having the same impact on most intrastate calls.

SUMMARY OF ARGUMENT

As the Illinois Supreme Court properly found, "[a] person simply cannot make or receive an interstate telecommunication without activating and participating in a complex network of interstate transmissions culminating in interstate communication. We believe that such interstate communication is interstate commerce. The very process of interstate communication is interstate commerce." Jurisdictional Statement, at 9a. Given this cognizance, the Illinois Supreme Court sought to apply the test enunciated by this Court in *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274 (1977), *reh'g denied*, 430 U.S. 976 (1977), under which a state is required to (1) tax no more than that portion of interstate commerce which is fairly allocable to activities within its borders; (2) not impose taxes that effectively discriminate against interstate commerce, regardless of the facial neutrality of such taxes; and (3) structure the tax so that it bears some reasonable relationship to the value of the services provided by and within the state.[8] But the court erred

[7] A small number of interstate calls, e.g., those from Moline to Davenport, are within a local calling area.

[8] The first prong of the test, that a state must have a sufficient "nexus" with the activity being taxed, is not in dispute here.

in its application of this test by failing to consider the real-world effects of the tax. This brief seeks to demonstrate the manner in which some of those real-world effects result in the tax violating all three of the above-listed elements of the *Complete Auto* test.

ARGUMENT

The failure of the Articles of Confederation was largely attributable to the inability of the government created under it to prevent destructive trade barriers from being erected by the several states. In fact, this weakness of the Confederation gave the main impetus to the Constitutional Convention, and the formulation at that Convention of the Commerce Clause. The principle aim of this Clause was to create among the now "united" States the world's first common market on a continental scale. "The very purpose of the Commerce Clause was to create an area of free trade among the several states." *McLeod v. J.E. Dilworth Co.*, 322 U.S. 327, 330 (1944).

Since at least *Gibbons v. Ogden*, 9 Wheat. 1 (1824), and *Brown v. Maryland*, 12 Wheat. 419 (1827), this Court's vigorous enforcement of the Commerce Clause has guaranteed that the United States would remain, economically, one nation. State governments, facing constantly changing technologies and patterns of trade, have repeatedly invented ingenious schemes for taxing commerce with non-residents more heavily than similar commerce involving residents; and this Court has just as repeatedly struck down all such schemes. See, most recently, *American Trucking Associations, Inc. v. Scheiner*, 107 S. Ct. 2829 (1987). Given the absence of substantial Congressional direction in this area, it has been principally this Court's steadfastness on the issue that has maintained the American common market by preventing impermissible barriers to interstate commerce to stand. The benefits to the nation of this long tradition of vigilance have been incalculably great.

This case involves another state scheme aimed at balkanizing the nation's economy—a tax that appears facially neutral, but which upon even a cursory analysis shows itself to be highly discriminatory against interstate commerce. For all commercial activities carried out by telephone, the tax systematically raises the relative cost of interstate as opposed to intrastate transactions, and awards Illinois business an unwarranted advantage in competing for Illinois trade. Ironically, this latest effort is aimed at precisely that sector of the economy which has, and will increasingly become, the irreplaceable electronic link among all Americans—the telecommunications industry.

I. The Telephone Tax is Unapportioned, and This Deficiency Cannot Be Corrected by the Credit Provided for Tax Payments to Other Jurisdictions.

As the Court below acknowledged, the Illinois telephone tax is completely unapportioned. Jurisdictional Statement, at 10a. The Supreme Court of Illinois excused this clear violation of the first *Complete Auto* standard on two grounds. First, on the basis of no record evidence, it concluded that no state other than Illinois could tax a call originating in Illinois and billed to an Illinois address. *Id.* Of course, this is not the case. For example, a state could constitutionally place a flat tax on each *usage* of a telephone instrument within the state, whether for sending or receiving a call. Such a tax would meet all facets of the *Complete Auto* test, and yet would necessarily result in multiple taxation of calls originating and billed in Illinois. Under *Japan Line Ltd. v. County of Los Angeles*, 441 U.S. 434 (1979), this example alone is sufficient to condemn the challenged law.

But although it neglected the obvious possibility for double taxation of calls originating in Illinois, even the Court below admitted that there was a real "risk of multiple taxation" with respect to that portion of the

telephone tax which applies to calls originating outside Illinois, and billed to an Illinois service address. Indeed, the Court noted that this risk is already a reality when the Illinois tax is considered along with taxes levied by two communities in Colorado. Jurisdictional Statement, at 12a. The lower Court's only answer to this dilemma was its reliance on the credit permitted against the Illinois tax under section 2004. But that reliance is misplaced.

First, while the Illinois telephone tax is collected from taxpayers by a "retailer" doing business in Illinois, it is apparently the taxpayer, and not the retailer, who must provide "proof" that he or she has paid a "tax properly due" to another jurisdiction. Section 2004. Thus it is at least questionable on this record whether a long distance company which transmits a call between Illinois and another jurisdiction has any obligation at all to deduct a tax paid to that other jurisdiction from the tax it collects from the Illinois taxpayer and remits to the state.[9]

But even assuming that such an obligation is imposed on telephone companies operating inside Illinois, it is unlikely that it would or could be uniformly observed by all telephone companies providing service to Illinois consumers. Today, most long distance carriers operate through their own lines across much less than the whole nation, interconnecting into areas they do not serve through some other carrier. Assume that the ABC Company provides long distance services to a Florida resident, and originates a call to Illinois, which is billed to an

[9] If individual taxpayers are required to file monthly or quarterly returns to apply for credit against taxes paid, then, for the average individual taxpayer represented by NTU, the credit provision of the tax becomes absolutely meaningless. The only way in which that provision can have any effect at all is for the credit to be calculated by the various long distance telephone companies when they calculate their customers' monthly bills. But, as shown below, even that prospect may be largely illusory in the circumstances of today's fragmented telephone industry.

Illinois service address. But the ABC Company does not operate in Illinois; to reach Illinois it must interconnect with the XYZ Company. Similarly, the XYZ Company does not operate in Florida. The ABC Company has no knowledge of the Illinois telephone tax, and no legal obligation under Illinois or any other law to calculate credits against that tax; it merely adds a Florida tax to the amount it bills the XYZ Company for the transmission. The XYZ Company has no knowledge of taxes imposed on long distance telephone calls originating in Florida—whether imposed by the State of Florida or by one or more of thousands of Florida municipalities—so it does not claim the credit. And of course, the Illinois taxpayer who receives the call has no knowledge of local Florida tax law, nor should he be expected to have such knowledge. In these not very unlikely circumstances, the credit supposedly allowed under the Illinois tax could not be anything other than hypothetical and illusory.

Electronic telecommunications are the messengers of modern times. If Illinois attempted to tax United Parcel Service on its entire charge for all packages picked up in the state, regardless of where they were to be delivered, that tax would fall before the Commerce Clause. *Japan Line Ltd., supra.* Yet telecommunications companies, whether they are in the telephone, telegraph, or electronic data transmission business, provide a service which for many purposes is functionally identical. Even under the loose standards adopted by the Court below, an unallocated tax on these services is equally invalid.

II. The Telephone Tax Discriminates Against Interstate Commerce.

"No State, consistent with the Commerce Clause, may 'impose a tax which discriminates against interstate commerce . . . by providing a direct commercial advantage to local business.'" *Boston Stock Exchange v. State Tax Comm'n,* 429 U.S. 318, 329 (1977). To decide the issue

of discrimination, this Court looks to the practical economic effects of a tax, not to the mere form of words used in the statute. *Complete Auto Transit, Inc. v. Brady, supra.* The validity of a tax will not be saved by showing that it might be constitutional under particular economic, geographic, or political conditions. A tax will be struck down if it is discriminatory, either on its face or as applied, under *any* reasonably conceivable circumstances. *Armco Inc. v. Hardesty*, 467 U.S. 638 (1984).

A concrete example will demonstrate that the telephone tax cannot meet this test. Consider two businesses, one located in Waukegan, Illinois and the other in Gary, Indiana: both businesses send catalogues to consumers in Chicago, and encourage those consumers to call in their orders by telephone. A five minute call to Waukegan (over a distance of about forty miles) costs a Chicago consumer (day rates, station to station) 26 cents, and incurs a telephone tax of 1.3 cents. A call to Gary from the same consumer (over a distance of about twenty miles) incurs a charge of $1.42, and a telephone tax of seven cents. The telephone tax penalizes the Gary catalogue business, and benefits the Waukegan business—precisely the result prohibited by the Commerce Clause. In fact, the tax paid on the call to Gary is more than *five* times as great as the tax on the call to Waukegan.[10] Moreover, the telephone tax does not have a compensating reverse effect when Gary consumers are substituted in this illustration for Chicago consumers. In that reverse case, neither call bears any tax, and the Gary catalogue business is not benefitted by the Illinois telephone tax.

[10] This result is not an accident resulting merely from the choice of cities made in constructing the foregoing example. Because local calling areas typically end at state boundaries (except where a single metropolitan area straddles the border), this result applies to nearly all comparisons of relatively short distance intrastate calls with interstate calls of an equivalent or lesser distance.

In *Westinghouse Electric Corp. v. Tully*, 466 U.S. 388, 395 n.9 (1984), this Court used "[h]ypothetical examples [to] demonstrate that similarly situated corporations . . . would face different tax assessments in New York depending on the location from which [each] shipped its exports." On the basis of such examples, the Court noted that this tax scheme, "not only . . . 'provide[d] a positive incentive for increased business activity in New York State' . . . but also penalize[d] increases in . . . shipping activities in other states." *Id.*, at 395-396. Similarly in this case, the telephone tax penalizes out-of-state businesses which wish to increase their sales or customer relations activities in Illinois by making access to those businesses more costly for Illinois consumers.

The discriminatory effect shown in the foregoing discussion cannot be justified by the fact that the dollar amounts at stake on each individual transaction are small, or by the argument that Illinois consumers would be more likely to interact with Illinois businesses in any event. This Court rejected these precise arguments in *Boston Stock Exchange, supra*, at 334, n.13. "Even if we did not conclude that . . . sellers are likely to rely on economic rather than geographical factors in choosing an exchange, [the challenged tax] would fall before the Commerce Clause. . . . [T]he Clause protects out-of-state businesses from *any* discriminatory burden on their interstate commercial activities." (Emphasis added.)

Beyond examples like the one above, however, the very core of this tax is its frontal assault on the most important instrumentality of interstate commerce. Over a century ago, in *Robbins v. Shelby County Taxing District*, 120 U.S. 489 (1887), this Court found that the imposition of a state "license fee" upon those engaged in the door-to-door selling of items to be delivered at a later time was in violation of the Commerce Clause. While such a tax appeared facially neutral, this Court found that interstate businesses would be more likely to use

this method of sale than local retailers, and therefore determined that the tax impermissibly discriminated against interstate commerce. Taxation of the only activity that would allow interstate businesses to compete was impermissible. "[T]he tax authorized by the State of Tennessee in the present case is discriminative against the merchants and manufacturers of other states. They can only sell their goods in Memphis by the employment of drummers and by means of samples; whilst the merchants and manufacturers of Memphis, having regular licensed houses of business there, have no occasion for such agents. . . ." 120 U.S., at 498.

There is at least an equally discriminatory impact here. Illinois has attempted to tax, without apportionment, the very instrumentality (interstate telecommunications) that is the central nervous system of every interstate business, and to do so by means of a tax which has a different and more burdensome effect on most interstate telecommunications than on most intrastate telecommunications. See, *supra*, at 7, 10. The Illinois telephone tax is essentially a tax on the privilege of communicating with people outside the state of Illinois, structured so as to reduce the demand for such communications, yet having little or no effect on the demand for intrastate communications.[11] It would be hard to conceive of a more effective or efficient deterrent to interstate commerce, or a more powerful incentive for the members of a single state or

[11] Since Illinois is a large state, the tax on a small minority of intrastate calls (for example from Chicago to Cairo) may approximate that on interstate telephone communications over equal or greater distances. But these are the exceptions, not the rule. The vast majority of intrastate calls are local free or message unit calls, or calls like that from Chicago to Waukegan which bear very low charges. Moreover, if the Illinois tax is approved by this Court, identical taxes in other, smaller states will be immune from constitutional challenge. Thus, even states like Rhode Island, where most of the population can make unlimited free calls to nearly the entire state, could adopt with impunity a tax modeled on the Illinois statute.

locality to deal solely with each other. Because the Illinois telephone tax discriminates against interstate commerce, it must be struck down.

III. The Tax Bears No Reasonable Relationship to the Value of Services Provided by the State of Illinois.

The fourth prong of the *Complete Auto* test requires a state tax on interstate activity to be "fairly related to the services provided by the State." 430 U.S., at 279. This test has been explained as requiring "the incidence of the tax as well as its measure [to be] tied to the earnings which the State . . . has made possible. . . ." *Commonwealth Edison Co. v. Montana*, 453 U.S. 609, 626 (1981). But the measure of the Illinois tax is in no way tied to the earnings and charges which Illinois has made possible in respect to interstate calling. Instead, calls which make more extensive use of out-of-state equipment are taxed more heavily than those which use more in-state equipment, as may be seen in the following examples:

A half hour call from Chicago to East St. Louis, Illinois originates with an Illinois telephone, is handled by an Illinois local operating company, an Illinois long distance company, and a second Illinois local operating company, and ultimately reaches an Illinois called party. In each of these five stages, this intrastate call involves persons and facilities enjoying the protections and benefits of Illinois law. This call costs $7.64, plus a telephone tax of 38 cents.[12]

A half hour call from Chicago to Honolulu originates with an Illinois telephone, is handled by an Illinois local operating company and long distance company, then is transferred to an out of state long distance company and a Hawaiian local operating company before it finally

[12] All charges in this example are day rate, station to station, AT&T.

reaches a called party in Hawaii. This call uses far *fewer* facilities having contact with Illinois than the call to East St. Louis. Yet this call bears a *higher* telephone tax of 56 cents, on a charge of $11.19.

A half hour call from Chicago to Bangkok, Thailand passes through the same Illinois equipment as the call to Honolulu, and like that call uses fewer in-state facilities than the call to East St. Louis. But the call to Bangkok uses a huge amount of additional telephone equipment located outside both Illinois and the United States. The cost of these extensive international facilities drives the price of such a call up to $35.46, plus a telephone tax of $1.77.

In short, the telephone tax imposes a higher *amount* of tax on activities with *fewer* in-state contacts. The value of services provided within Illinois is substantially less in the case of the calls to Honolulu and Bangkok than in the case of the call to East St. Louis, but the tax imposed is higher.

But even if one assumes (contrary to fact) that the value of the Illinois services involved in each of these calls is *the same*, the tax rate imposed is still higher when the call is made to a place outside Illinois. For example, the tax on the call to East St. Louis constitutes only *5 percent* of the charge attributable to use of the Illinois facilities actually involved in that call; by contrast, the telephone tax on the call to Honolulu constitutes *7.3 percent* of the same $7.64 charge, while the tax imposed on the call to Bangkok constitutes *23 percent* of that same charge. In *Scheiner*, *supra*, this Court held that, "when the measure of a tax bears no relationship to the taxpayers' presence or activities in a State, a court may properly conclude . . . that the state is imposing an undue burden on interstate commerce." 107 S. Ct. at 2844. As the foregoing examples show, this is clearly the case with the telephone tax.

CONCLUSION

The *Complete Auto* test is in the conjunctive, and not in the "quasi-disjunctive" that the lower court attempted to apply; a tax must meet each prong of the test to pass constitutional scrutiny. Under these standards, and as applied to the various types of charges described above, the Illinois telephone tax is blatantly unapportioned, discriminatory against interstate communication, and not fairly related to the services provided by the State of Illinois. For these reasons, and for the reasons set forth in the Briefs of Appellants, this Court should reverse the decision below, and find the Illinois telephone tax unconstitutional.

Respectfully submitted,

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(9) (8)

Nos. 87-826 and 87-1101

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

JEROME F. GOLDBERG and ROBERT MCTIGUE,
Appellants,
v.
ROGER D. SWEET, DIRECTOR OF THE ILLINOIS DEPARTMENT OF REVENUE, *et al.*,
Appellees.

GTE SPRINT COMMUNICATIONS CORPORATION,
Appellant,
v.
ROGER D. SWEET, DIRECTOR OF THE ILLINOIS DEPARTMENT OF REVENUE, and JEROME COSENTINO, TREASURER OF THE STATE OF ILLINOIS,
Appellees.

On Appeal from the Supreme Court of Illinois

BRIEF OF THE NATIONAL CONFERENCE OF STATE LEGISLATURES, U.S. CONFERENCE OF MAYORS, INTERNATIONAL CITY MANAGEMENT ASSOCIATION, NATIONAL ASSOCIATION OF COUNTIES, NATIONAL GOVERNORS' ASSOCIATION, NATIONAL LEAGUE OF CITIES, AND COUNCIL OF STATE GOVERNMENTS AS *AMICI CURIAE* IN SUPPORT OF APPELLEES

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QUESTION PRESENTED

Whether the Commerce Clause precludes Illinois from imposing an excise tax on the retail purchase of interstate telephone calls involving an Illinois party and charged to an Illinois customer, when the same tax is levied on the purchase of intrastate calls and full credit is allowed for a similar tax paid to other States.

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INTEREST OF THE *AMICI CURIAE*

The *amici*, organizations whose members include state, county, and municipal governments and officials throughout the United States, have a compelling interest in legal issues that affect state and local governments.

Appellants are attempting to invalidate an Illinois tax as it applies to retail interstate telecommunications services. The tax, which is also imposed on all intrastate calls, is levied on calls initiated or received in Illinois and charged to an Illinois service address. The tax provides a credit to avoid multiple taxation.

Amici are concerned about this case not only because of its importance to Illinois,[1] and to the other States that have a similar tax,[2] but also because the course advocated by appellants would substantially impair the States' ability to tax electronic communications and would lead the Court—and the States—back into the quagmire that its recent unanimous decision in *D.H. Holmes Co. v. McNamara*, 108 S.Ct. 1619 (1988), left behind.

In today's marketplace, almost all businesses are in some sense engaged in interstate commerce. Naturally,

[1] As of July 27, 1987, the amount of this tax paid to Illinois was at least $142 million, and the tax was being collected at a rate of $10 million a month, or about $120 million annually. See Brief for Appellants Goldberg and McTigue at 5.

[2] Appellants have identified ten States that impose taxes of some type on interstate telephone calls purchased in the State. See Brief for Appellant GTE Sprint App. A.

most businesses would like to use that connection to shelter their activities from state taxation by claiming that a tax violates the Commerce Clause. The States, however, are facing increasing responsibilities because of federal budget constraints and the current trend in both the Executive and Legislative Branches of the federal government to relinquish to the States responsibilities that had been borne by the federal government. The elected officials of each State need the freedom to acquire the revenue to meet these responsibilities from all the available sources.

The States are especially concerned that they not be deprived of the power to tax the new products and activities that the telecommunications, computer, and information industries are developing. These new activities sometimes involve the interstate "movement" of electronic impulses over huge distances at the speed of light under remote control, in sharp contrast to the conventional "movement" of cargo, passengers, and vehicles. They are a potentially important source of future state revenues which should not be foreclosed unless there is a clear constitutional necessity for doing so.

Illinois has selected a rational, uncomplicated, and practical taxing approach that requires purchasers of interstate telecommunications services to bear their fair share of the costs of government services. It is based on the charges to Illinois customers for calls involving Illinois parties. To avoid duplicate taxation, it provides a credit for other States' taxes.

Amici believe that, if appellants were to prevail here, the result would be either to exempt the purchase of interstate telephone conversations from state taxation altogether or to impose on all state legislatures constraints so complex, burdensome, and costly for customers, vendors, and States alike, that States would be effectively precluded from utilizing such taxes. The suggestion that the only valid way to tax such conversations is for each State through which a call "passes" to have a toll gate at its boundaries, and assess a tax corresponding to its par-

ticular contribution to the transmission of that particular call, ignores the reality of how a modern long distance telephone conversation is bought and transmitted.

Neither Congress nor the Court has mandated a single system of taxation to be used by all States. Instead, the Court has developed the four-part test set out in *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977), and applied in the Court's unanimous decision this Term in *Holmes*. The test recognizes that, in our federal system, each State can make different taxing choices based on widely varying political and economic conditions.

Amici believe that the decision of the Illinois Supreme Court upholding the tax is correct. It allows the States to require in-state purchasers of interstate telephone conversations to help meet the costs of state government. Reversal would require other taxpayers, including customers of other taxed businesses with multistate aspects, to subsidize this growing and profitable form of business activity. Thus, because this Court's decision will have a direct effect on matters of prime importance to *amici* and their members, *amici* submit this brief to assist the Court in its resolution of the case.[3]

STATEMENT

The Statements set forth in the briefs of appellants and appellees adequately cover the specific history of this case. However, *amici* consider many of the arguments of appellants and their *amicus curiae*, National Taxpayers Union, to be based on factual assumptions that are not valid. *Amici* thus believe that the Court would be assisted by a further explanation of the nature of the business activity at issue here, as it occurs not just in Illinois but throughout the Nation.

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[3] Pursuant to Rule 36 of the Rules of the Court, the parties have consented to the filing of this brief. Their letters of consent have been filed with the Clerk of the Court.

1. *The structure of the long distance telephone industry.*[4] The typical telephone subscriber is a customer of a local telephone company, which in turn is part of a regional company created in the breakup of AT&T, part of a national holding company (such as GTE), or an independent company.[5] The local company handles all dialed calls within its local service area, and in some States handles all toll calls in a wider market area. In most States, the local or regional telephone company has competition for some or all of the intrastate toll calls from one point in its system to another, and, if it operates in more than one State, has competition for all of the interstate long distance business within its service area.

The long distance industry was a $60 billion industry in 1986,[6] and some of the larger players spend tens of millions of dollars in marketing and advertising aimed at securing customers throughout the Nation.[7]

AT&T is still the largest of the long distance carriers, but there are now dozens of others, such as Sprint[8] and

[4] See generally U.S. Dept. of Justice, *The Geodesic Network: 1987 Report on Competition in the Telephone Industry* ("DOJ Study"), at 1.2-1.9.

[5] This entire field is infected with an ever-growing lexicon of acronyms, the proliferation of which makes them all less and less useful. Thus the local companies are LECs (local exchange carriers), including 22 former BOCs (Bell Operating Companies) owned by seven holding companies called RBOCs (regional Bell operating companies). They operate in 161 LATAs (Local Access Transport Areas) and are connected to one another by ICs (interexchange carriers) which have POPs (points of presence) in the LECs' LATAs. *Amici* will attempt to use descriptive English words as much as possible.

[6] DOJ Study at 3.5.

[7] DOJ Study at 3.4.

[8] Sprint was wholly owned by GTE. As a result of an arrangement between GTE and United Telecommunications, Sprint has been succeeded by U.S. Sprint, jointly owned by the two companies. See *Hold the Phone,* Forbes 52 (June 13, 1988).

MCI, which have a growing share of the long distance business, both interstate and intrastate. These carriers transmit their long distance calls through a wide variety of methods. Some of them have invested billions of dollars in their own transmission networks, including conventional land lines, microwave networks, satellite equipment and channels, and fiber optic lines. Others are basically resellers, buying transmission and connection services at wholesale from other carriers, including AT&T and the local companies, and selling them at retail to individual callers. Because the local telephone companies (with a few exceptions) are the exclusive source of connection to individual subscribers, the long distance carriers must, at each end of each long distance call, rely on the local companies to carry the call from the point at which the long distance lines connect into the local system to and from the parties to the call.

Every local telephone subscriber can select a long distance retailer to be his primary long distance carrier, *i.e.,* the carrier that automatically gets the direct-dialed long distance business from that telephone when a long distance number (other than some toll calls in some local market service areas) is dialed. A subscriber can use another long distance carrier by dialing a special code or an access number for the carrier (originally a local number and now usually an 800 number) to reach a regional or national switching center, which puts the long distance carrier's dial tone or operator on the line for completion of the call, whether intrastate or interstate.

2. *The mechanics of long distance calling.* The networks of paths and switching points that constitute a long distance system are not at all like highways or rail lines or other ordinary routes of physical movement. Instead, these networks consist of "geodesic" structures, webs of linked paths capable of switching the course of signals at each crossing or "node."[9] By way of illustration, a triangle with three nodes offers two routes to get

[9] See DOJ Study at 1.2-1.3.

from one corner to a second—one direct, and one via the third corner. A network with thirty nodes connecting its various paths offers *billions* of routes to get from any one point to any other.[10] Once a telecommunications network exists, there is no noticeable loss or delay from using any available path. Thus, any time that a direct path is full or not working at peak efficiency, any other route, no matter how indirect—and without any regard for state boundaries—can be utilized instantaneously, even by switching paths during a call. In some areas, the network is built with very few cross paths, but with most of the paths arrayed like spokes on a hub, so that calls from one point on the rim to another nearby in-state point must travel all the way into the hub—which may well be in another State—and back out on the next spoke.[11]

Microwave and satellite transmission add further variations. A signal travelling from one microwave tower to the next may go "through" a State but never touch anything in it. A satellite transmission may leave the building the caller is in on one coast and never touch the ground again until it is received at a satellite dish on the building housing the other party on the other coast. Even a call between two parties in the same State might take a similar route—going up at one end of the State, coming down at a dish in a nearby State, and then coming back into the State by wire or microwave.[12]

In short, rather than having a predictable, or "necessary," course, telephone calls literally travel every which

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[10] *Id.* at 1.18, 2.26.

[11] For example, a long distance telephone call from Kittery, Maine, to Portland, Maine, travels through Portsmouth, New Hampshire. See Attachments A-1–A-9 to Exhibit filed October 4, 1982, by AT&T in *United States v. Western Electric Co.*, Civil Action No. 82-0192 (D.D.C.)

[12] Before Illinois began to allow competition for certain intrastate phone service, GTE and other non-Bell carriers used to route some of their Illinois-to-Illinois calls via out-of-state points to give them "interstate" status. See Krohe, *Rules for a Revolution: Telecommunications in Illinois,* Illinois Issues 6, 8 (Sept. 1984).

way. Ostensibly intrastate calls frequently are routed through other States and can go out into space over other States or even other countries. Interstate calls may travel an almost unlimited number of radically different routes through large numbers of States to reach their destination. The long distance segment of an intrastate call may have very little contact with that State, while an interstate call of the same straight-line distance may travel most of its course through the State. Since each call may take a different course (or multiple courses) through a large number of States, or no States, it is virtually impossible to keep track of the precise route of each call even if there were a reason to do so, for the cost of identifying and recording each such segment of each call would be prohibitive in relation to the cost of the call.

Thus, the assumption[13] that the purchaser of a long distance telephone call has his cargo of electronic impulses transported over the shortest route to its destination along a defined path using a particular mode of transmission, like a trucking or rail customer, is totally inconsistent with the technology of today's telephone industry. The purchaser of a long distance telephone call simply buys from the vendor a single end product: a conversation with a distant person. The purchaser cares not a whit which States the call goes through, whether it zig-zags through thousands of nodes or goes in a straight line, whether it goes down the spokes of a hub and back again, or up into space and back again, as long as the quality is good and the price is right.

3. *The cost of long distance calls.* Appellants also assume that there is a simple, proportional relationship between the distance separating the parties to a call and the price of the call.[14] In fact, over the period covered by this case, the price of calls throughout the Nation has

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[13] See, *e.g.*, Goldberg Brief at 31, 34.

[14] *Id.* at 33-34.

varied as widely as the routing and technology for those calls. Differences in history, competition, regulation, market strategy, and cost levels for long distance providers have produced a price structure that is constantly changing, difficult to comprehend, and anything but regular. Since 1985, in many places, including the Washington, D.C., metropolitan area, the price of some intrastate toll calls has been significantly higher than the price of some interstate calls covering much longer distances. And many shorter distance interstate calls are priced higher than longer distance interstate calls.[15] Sometimes the price of a shorter intrastate call has been greater than the price of other intrastate calls of greater distance.[16]

Since much of the cost of a typical long-distance call is at the ends, and for billing and other non-transmission costs, rather than for the long distance transmission, and since some long distance calls are handled by satel-

[15] The current telephone book shows the rate for a daytime call within Maryland of 71 miles at 54 cents for the first minute and 37 cents for additional minutes, while a call from Maryland to Virginia of 292 miles costs 51 cents and 35 cents, respectively. See 1987 C & P Telephone Prince George's County White Pages at pp. 26-27. Calls from Arlington, Virginia, to various points are priced as follows:

Stafford, Va.	30 mi.	.44 1st min.	.29 add. min.
Leonardtown, Md.	45	.48	.28
Central Ohio (419)	400	.25	.24
No. Calif. (916)	2800	.31	.27

[Va. and Md. rates per 1988 C & P Virginia White Pages at pp. 26-27; Ohio and Calif. rates per U.S. Sprint Customer Service. Mileage approximate, from Rand McNally Road Atlas, pp. 3, 99 (1984)].

[16] *E.g.*, the cost in cents for a call from Chicago to Schaumburg, Ill., in 1985 was 22 for the first minute and 14 for additional minutes. A call to Elk Grove Village, closer to Chicago, cost 30 and 19. A call to Waukegan, about twice as far from Chicago as Elk Grove was 26 and 16. See 1985 Illinois Bell Chicago Telephone Directory at p. 27.

lite, which is not distance sensitive,[17] the distance between the parties may be a much less significant factor in the cost of a call than the form of service chosen (direct dial, credit card, collect, person-to-person); and the spread between the price of calls to destinations at drastically different distances is steadily diminishing.[18]

Whatever the total retail price for a call, the buyer pays the cost of both ends, whether the distance between the parties is short or long, and whether the other end is in the same or a different State. When a customer in Illinois purchases a conversation with a person in New York from the long distance carrier, the price includes all three components of the service—the Illinois end, the multi-state (or no-State) middle, and the New York end —just as the purchase of a Chicago-Waukegan call includes both ends and the (possibly interstate or outer space) middle of that call.[19] The person in Illinois who buys the call is purchasing the whole product from the vendor, who assembles the many pieces of multi-state activity necessary to create the product, just as the Illinois buyer of a book buys from a Chicago bookstore the Michigan pulp, which went into the Wisconsin paper, which, combined with the Ohio ink, was used in New Jersey to print the New York-edited text written by the Vermont author living in Florida.

[17] See DOJ Study at 1.3, 3.8; E. Ploman, *Space, Earth and Communication* 63 (1984) (satellite communication is "'cost distance' insensitive").

[18] Current Sprint prices for the first minute of a telephone call from Washington, D.C., include 24 cents to Baltimore (37 mi.), and to New York (229 mi.), 25 cents to Rochester, NY (296 mi.), and to Boston (414 mi.), 28 cents to St. Louis (696 mi.), 29 cents to Chicago (590 mi.), 30 cents to Miami (919 mi.) and Salt Lake City (1839 mi.), and 31 cents to Denver (1464 mi.). The Sprint surcharge for using a credit card is 55 cents. The mileage figures are airport to airport miles from the Official Airline Guide (June 15, 1988).

[19] The only exception is certain large volume users, which may have direct connections to a long distance carrier at one or both ends of the call.

But, unlike the book, each copy of which probably has the same multi-state origins, each call, even between the same parties, can take very different routes. Nevertheless, the purchaser of retail telephone services does not pay a different price for a particular call because it took a roundabout route through the network, or went 22,000 miles into space and back again, or because it went by fiber optics instead of microwave. The long distance carrier itself treats the entire point-to-point conversation as the essence of the purchase and charges the same price at retail for that point-to-point conversation regardless of how or how far it travels to get from point to point. Under present practice, neither the vendor, nor the customer, nor the many States through which a call may travel, record or care about the particular route of a single call. And, until this case, no one has suggested that they should.

INTRODUCTION AND SUMMARY OF ARGUMENT

Neither the text of the Commerce Clause nor the interpretive rulings of this Court impose on the States any particular form of tax strategy. States may select from a variety of tax mechanisms, including excise taxes on specific types of purchases, gross receipts taxes on business activity, or income taxes. The fact that the purchases, receipts, or incomes on which such taxes are levied derive in part from activities with multi-state aspects does not render them unconstitutional. In fact, in today's commercial world, there is virtually no activity that does not have an interstate dimension, and any rule that erected serious barriers to the state taxation of such activities would present an ominous threat to the viability of the federal system.

All that the Constitution demands of such state taxes is that they operate fairly and not create discriminatory impediments to the free flow of interstate commerce. This Court listed in *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274 (1977), and explained in *D.H. Holmes Co. v. McNamara*, 108 S.Ct. 1619 (1988), the

factors to be considered in making that assessment: adequate nexus with the taxing State, apportionment among States if the tax is imposed in more than one State, no discrimination against out-of-state activities as compared with in-state activities, and some general benefit to the taxpayer from the taxes paid.

The Illinois tax on telecommunications at issue in this case more than meets those standards. The tax is imposed only on calls that are linked closely with Illinois because they are made either to or from Illinois and are charged to an Illinois customer of the retailer of such calls. In the nature of the long distance telephone business, this means that the vendor offers his retail long distance services in Illinois and has or purchases transmission facilities in the State. Where the taxpayer would be subject to a tax on the same call in another State, Illinois makes the maximum possible allowance by providing a full credit for taxes paid to any other State. Thus, Illinois goes beyond the requirement of apportionment by ceding its taxing power completely to the extent of the other tax.

The question of discrimination does not even arise because Illinois imposes the same percentage tax on intrastate and interstate calls. A prospective customer making a $2.00 call to place an order with an out-of-state factory will pay the same tax (10 cents) as he would if he placed the same priced call to an Illinois supplier. Similarly, there is no state benefit problem here. While the Court requires only a general benefit to the taxpayer, here both the taxpayer and the vendor have a presence and activity in Illinois and thus both are benefitted by the state services that the telephone tax supports.

The unanimous decision this Term in *Holmes*, issued after the filing of appellants' briefs here, should resolve any doubts as to this case. *Holmes* involved a situation where the item subject to the tax had much less nexus with the taxing State, the vendor had none, and the state benefits thus went only to the taxpayer and not the vendor.

Amici believe that the unanimity and clarity of *Holmes* should be preserved. *Holmes* has simplified a difficult area, and promotes the consistent view of this Court, essential to the health of the federal system, that the States must be given adequate flexibility to develop taxing mechanisms to support the growing burden of public services that they are called upon to provide. The broad variety of communication and information products is a rapidly growing source of business activity which should not be immunized from paying its fair share of state taxes. As this industry expands, the Court should allow the States to develop their own means of moving with the times consistent with *Complete Auto* and *Holmes.* If substantial problems arise, the Court will have ample opportunity to resolve them. Here there are no real problems that need repair. Nevertheless, appellants would have this Court—in anticipation of speculative and avoidable future problems—become a super state legislature and impose its own set of rigid rules which will hobble the States and impose costly new administrative obligations on the telecommunications industry.

In fact the remedies suggested by the appellants would worsen the situation they now face. One appellant would have this Court require use of a "unitary business/formula apportionment" technique to figure each State's taxable share of telecommunications activity. Apart from the fact that the Court has not made any one form of tax mandatory, the selection of that particular form, which is valid, but complex and hotly contested, to the exclusion of all others, hardly seems reasonable. The other appellants would have the Court require a state-by-state breakdown of each and every call, so that each State on the route can assess a tax commensurate with its particular contact with the call. Since a single call may have different types of contacts with dozens of States, may take a route different from another call between the same two points, and may even switch routes in mid-call, this impractical alternative appears counter-

productive for all concerned and emphasizes the rationality of Illinois' selection of the tax involved in this case.

Illinois does not attempt to tax all calls with an Illinois participant, as appellants apparently would allow it to do. It taxes only those calls that have both that nexus, and, in addition, a purchaser in the State. If a call to or from Illinois is charged to a subscriber elsewhere, the call is not subject to the Illinois tax. Thus, if other States adopt Illinois' system, there would be no multiple taxation, not even the permissible level of minor overlap which this Court has allowed. A call in either direction between State A and State B will be taxed in State A if it is charged to a subscriber in A and taxed in State B if it is charged to a customer in B. That is as simple and reasonable an arrangement as one can imagine in this complicated field. It is beyond *amici*'s comprehension why any taxpayer or vendor would want to change that system, except in hopes that the alternative would be so labyrinthine that it would discourage States from taxing telecommunications at all.

Neither the Constitution nor this Court is a suitable instrument for that kind of mission. *Complete Auto* and *Holmes* fully support the Illinois Supreme Court's decision, and that decision should be affirmed.

ARGUMENT

I. THE UNANIMOUS DECISION IN *D.H. HOLMES,* APPLYING *COMPLETE AUTO,* CONTROLS THIS CASE.

The lower court and the parties agree that the general principles set forth in Justice Blackmun's opinion for a unanimous Court in *Complete Auto*, 430 U.S. 274 (1977), are relevant here. In *D.H. Holmes Co. v. McNamara*, 108 S.Ct. 1619 (1988), the Chief Justice wrote for a unanimous Court that "*Complete Auto* abandoned the abstract notion that interstate commerce 'itself' cannot be taxed by the States. We recognized that, with certain restrictions, interstate commerce may be required to pay

its fair share of State taxes." *Id.* at 1623. In *Complete Auto,* the Court ruled that a state tax does not offend the Commerce Clause if it is applied to an activity with a "substantial nexus with the taxing State, is fairly apportioned, does not discriminate against interstate commerce, and is fairly related to services provided by the State." 430 U.S. at 279. But in *Complete Auto* those criteria were merely identified, and not contested or applied, leaving open many questions of application and interpretation.

In most of the cases interpreting *Complete Auto* since that unanimous decision in 1977, the Court's struggles with those concepts have left it divided, frequently intensely so. *See, e.g., Mobil Oil Corp. v. Commissioner of Taxes of Vermont,* 445 U.S. 425 (1980) (majority opinion joined by six Justices; one dissenting; two not participating); *Commonwealth Edison Co. v. Montana,* 453 U.S. 609 (1981) (opinion of the Court joined by five Justices; one Justice ("with considerable doubt") concurring; three dissenting).[20] But this Term in *Holmes,* the Court again achieved unanimity in this field. The opinion by the Chief Justice provides clear and concise guidance for the application of *Complete Auto* in a context more problematic than this case. The conclusion in *Holmes* makes manifest that taxes like the Illinois tax at issue here fall well within the scope of valid state taxing power.

In *Holmes,* Louisiana imposed a 3% "use" tax on the taxpayer's "distribution" in Louisiana of catalogs purchased, designed, and printed in other States and mailed into Louisiana. The taxpayer, D.H. Holmes Company, owner of thirteen department stores in the State, argued that the application of the use tax violated the Commerce Clause. The state court found that the catalogs had

[20] *See also American Trucking Ass'ns, Inc. v. Scheiner,* 107 S.Ct. 2829 (1987) (5-4 decision); *Tyler Pipe Indus., Inc. v. Washington Dept. of Revenue,* 107 S.Ct. 2810 (1987) (4 separate positions).

"left the stream of interstate commerce" when they "landed" in mailboxes in Louisiana. 108 S.Ct. at 1622. This Court, however, held that *Complete Auto* dispensed with the notion that interstate commerce itself cannot be taxed, and thus "it really makes little difference for Commerce Clause purposes whether appellant's catalogs 'came to rest' in the mailboxes of its Louisiana customers or whether they were still considered in the stream of interstate commerce." *Id.* at 1623. Thus the Court analyzed the validity of the tax under the Commerce Clause on the basis of the *Complete Auto* criteria, and in doing so articulated clearly the reasons why the Illinois tax challenged here must be found valid.

A. The Illinois Tax Is Applied To An Activity That Has A "Substantial Nexus With The Taxing State."

In *Holmes,* nexus was hotly contested because the use tax was levied as a result of distribution by mail of items whose origins were entirely out of state. Nevertheless, this Court found "'nexus' aplenty" (108 S.Ct. at 1624), not only because of the distribution of Holmes' catalogs in Louisiana, but also because the taxpayer itself had "significant economic presence in Louisiana," had "many connections with the State," and received "direct benefits" from the State in conducting its business. *Ibid.*

In this case, appellants concede nexus, and for good reason. There are at least four independent bases for finding nexus here. First, every call taxed by Illinois originates or terminates in Illinois, which means that the taxed activity itself has a substantial connection with the State. Second, the key transaction, the *sine qua non* of that activity, is the agreement of an Illinois customer to purchase the call; it is also inherently an Illinois-connected event. Third, the subscriber making the purchase and subject to the tax resides or conducts a business in Illinois and thus receives benefits from the State. Finally, the vendor certainly has, to use the Court's felicitous phrase, "many connections with the State" (108

S.Ct. at 1624).[21] Not only does each call it sells and completes there constitute a connection with the State, but the "POPs" (points of presence) that connect it to the various local calling areas in the State, its marketing efforts in the State, its ability to be accessed directly on the telephones in the State, and its involvement in the regulatory process of the State,[22] each establish a separate nexus for the vendor, even if the "nexus aplenty" of the taxpayer were not more than sufficient. In short, this case follows *a fortiori* from *Holmes*, where the activity nexus was weaker and the vendor of the catalogs had no apparent nexus at all. Here the activity, the purchase, the taxpayer, and the vendor all have solid and extensive nexus to the taxing State.

B. The Illinois Tax "Is Fairly Apportioned."

In *Holmes*, the State's tax was a fixed percentage of "the cost price" of the item used or distributed in the State.[23] There was no attempt to determine or adjust for the relative proportion of in-state and out-of-state value in the item or—with one exception—to treat the item purchased out-of-state any differently than if it had been an item purchased in-state and subject to the sales tax. That exception was the section of Louisiana law which provided that a "credit against the use tax . . . shall be granted to taxpayers who have paid a similar tax

[21] It is worth noting the source of GTE's present financial interest in the case. While the state law requires the telephone carrier to pay the tax if the subscriber does not, in this case the absence of payment by GTE's subscribers appears to be the result of an administrative deficiency on GTE's part. See Goldberg Brief at 3 n.1.

[22] Sprint's current Monthly Bill Form refers to various rules of "your state's Public Utility Commission" four times.

[23] Although the use tax speaks in terms of tangible personal property (*see Holmes*, 108 S.Ct. at 1621 n.1), which the catalogs undoubtedly were, the complementary sales tax, which covers sales of services, treats printing as a sale of services. See La. Rev. Stat. Ann. § 47:302(C); § 47:301(14)(d) (West 1988).

upon the sale or use of the same tangible personal property in another state." 108 S.Ct. at 1623-24. On this basis, the Court had "no doubt" that the apportionment test was satisfied: "The Louisiana taxing scheme is fairly apportioned, for it provides a credit against its use tax for sales taxes that have been paid in other States." *Id.* at 1623.

The situation in the instant case is indistinguishable in this respect, and the Illinois Supreme Court was prescient in using almost identical language to make the same finding. That court found that the apportionment test of *Complete Auto* was met here because the Illinois tax on the purchase of interstate telephone calls "provides a credit against any tax due from a taxpayer who has paid two or more taxes on the same interstate telecommunication." J.S. App. in No. 87-826 ("Goldberg App.") at 13a.[24]

In finding that the Louisiana tax was fairly apportioned, the Court in *Holmes* mentioned only one other factor: that "Louisiana imposed its use tax only on the 82% of the catalogs distributed in-state; it did not attempt to tax that portion of the catalogs that went to out-of-state customers." *Id.* at 1624. Similarly, Illinois makes no attempt to apply its tax if there is either no Illinois party or no Illinois purchase. The tax applies only to a person in Illinois who purchases retail telecommunications originated or received in Illinois. Goldberg App. at 29a; Ill. Rev. Stat. ch. 120, § 2004 (1986).

Thus, while there might be other ways of meeting the fair apportionment test, the two criteria set forth in

[24] As this Court noted in *Holmes*, the Louisiana statute included a provision "instructing that 'there shall be no duplication of the tax.'" 108 S.Ct. at 1624. The Illinois law prefaces its credit provision with a similar statement of its purpose: "To prevent actual multi-state taxation of the act or privilege that is subject to taxation under this paragraph . . . ." Goldberg App. at 29a-30a; Ill. Rev. Stat. ch. 120, § 2004 (1986). *See also Tyler Pipe*, 107 S.Ct. at 2821 ("a credit for . . . taxes paid to other States would presumably cure the discrimination").

Holmes—a credit "to taxpayers who have paid a similar tax" and absence of any effort to tax activities with no in-state component—are fully satisfied here.

C. The Illinois Tax "Does Not Discriminate Against Interstate Commerce."

Holmes requires only that the tax applicable to the out-of-state purchase be the same as that on an in-state purchase. Since the Louisiana tax was "equal" to the sales tax on in-state purchases, *i.e.*, the same percentage of the value of the taxed item, the Court found that the State's "tax structure . . . does not discriminate against interstate commerce." 108 S.Ct. at 1624. There is no suggestion of any requirement, urged by appellants here, that the tax on the interstate transaction must be less, because it contained out-of-state value, or that the tax on the in-state transaction must be more because it contained more in-state value.[25]

Undoubtedly a catalog ordered, designed, printed, packed, and shipped within the State might well have higher in-state content; but the Court plainly did not view the absence of a differential in the tax formula as discrimination against interstate commerce in the constitutional sense. The Court did not consider it necessary to venture into this interstate tax quagmire, in part, one could suppose, because of the impact on the Court's caseload if each State were required, at peril of violating the Commerce Clause, to vary its tax on each transaction, activity, or item with out-of-state value so as to reconcile each of them with every other.[26]

[25] The Court has never suggested that state sales taxes may be imposed only on the value added in the State or attributable to a transaction within the State. That type of tax is a value added tax, not a sales tax. See generally C. McLure, Jr., *State and Local Implications of a Federal Value Added Tax* 2-3 (Academy for State and Local Government, Jan. 1987). Among the States, only Michigan has a value added tax. Mich. Comp. Laws Ann. §§ 208.1-208.145 (West 1986).

[26] Presumably, this evaluation would be required as well for those "intrastate" calls that travel to out-of-state switching points or on out-of-state paths, or on supra-national paths via satellite.

Again, there can be no doubt that the Illinois tax conforms to the *Holmes* explanation of the *Complete Auto* discrimination test. The Illinois tax on the purchase of interstate calls is "equal" to that on the purchase of intrastate calls: 5% of the gross charge. Goldberg App. at 29a; Ill. Rev. Stat. ch. 120, § 2003 (1986). The rate of the tax on the gross retail purchase price of a ten-minute call with a person one hundred miles distant will be exactly the same, whether that person is in-state or out-of-state, and the absolute amount will be the same, if the retailers of those calls charge the same gross price.

If the price of an intrastate call is higher than the price of an interstate call of equal or greater reach and duration (see pp. 7-9, *supra*), then the tax will be higher on the intrastate call. Similarly, the price, and therefore the tax, on two identical calls—either interstate or intrastate—bought from two different carriers may be different if, in their competitive wisdom, they set different rates.

But none of these differences in the price-based tax goes to the issue of the constitutional validity of the tax. Although the retailer may be buying the raw components of the completed product in different places and at costs that vary from call to call and sometimes within a call, and may be obtaining a different profit margin on different calls between identical end points, the customer is buying a complete conversation for one price and paying one retail tax. The customer pays the same tax on the same price call whether that call goes between two in-state points via another state or via outer space, or between an in-state and out-of-state point over long lines and switching machinery that is all in-state.[27] *Holmes* makes clear that the Commerce Clause requires no more.

[27] This can happen in Illinois when a call from one end of the State goes to a local exchange carrier in a multi-state metropolitan area. It can happen elsewhere if all the switching for a multistate area is done in one State, so that the "work" for a call from that State to one of the other States is almost completely done in the originating State.

D. The Illinois Tax "Is Fairly Related To Services Provided By The State."

In *Holmes*, the catalogs at issue were the result of creative and production processes outside the taxing State until the final act of delivery by U.S. mail. Thus the Court was faced with the argument that Louisiana provided no services whatsoever in connection with the creation and distribution of the taxed goods.

Faced with a similar contention on the nexus issue, the Court relied in part on the in-state distribution process itself as a basis for finding the requisite contact. But on the "benefits" issue, the Court made clear that the *taxpayer's* receipt of general advantages or benefits from the State—including the general benefits to the public of tax-supported safety and transportation services unrelated to the specific taxed item or transaction—was sufficient. "Louisiana provides a number of services that facilitate Holmes' sale of merchandise within the State: It provides fire and police protection for Holmes' stores, runs mass transit and maintains public roads which benefit appellant's customers, and supplies a number of other civic services from which Holmes profits." 108 S.Ct. at 1624. While the Court recognized that "many others in the State benefit from the same services," it concluded that the tax on the catalogs "is related to the advantages provided by the State which aid appellant's business." *Ibid.*

There is not the slightest hint in the *Holmes* opinion that the state services did, or needed to, relate to the particular process of creating or distributing the taxed item—*i.e.*, benefit the out-of-state catalogs. Nor is there any suggestion that meeting the benefits test depended on an analysis of the relative magnitude of the in-state to out-of-state "burden" created by the catalogs, as is urged by appellants here. On the contrary, if that had been the test, the catalogs in *Holmes* would surely have failed it.

Appellant GTE's problem proceeds from its description of the test: "fair relation to the services Illinois provides *the taxed activity*." GTE Brief at 47 (emphasis added).

Of course, the emphasized words do not appear in *Complete Auto*. In fact *Commonwealth Edison Co. v. Montana*, 453 U.S. 609 (1981), the very case that GTE cites, makes clear that GTE's approach is based on "the incorrect assumption that the amount of state taxes that may be levied on an activity connected to interstate commerce is limited by the costs incurred by the State on account of that activity." *Id.* at 627 n.16. On the contrary, "interstate commerce may be required to contribute to the cost of providing *all* governmental services, including those services from which it arguably receives no direct 'benefit'." *Id.* at 628.[28] Here there is no question that the taxpayer (as well as the vendor) benefits from Illinois services financed in part by the tax. As the nexus discussion above (pp. 15-16) demonstrates, since the taxpayer subscribes to telephone service in Illinois, makes an Illinois purchase of the service, and generally is in Illinois participating in the particular conversations purchased, all of the general civic benefits provided by the State and supported in part by the telecommunications excise tax benefit the taxpayer.[29] Moreover, even though, as *Holmes*

[28] The dissent in *Commonwealth Edison*, even though disagreeing with the majority on the fourth prong of *Complete Auto* because it found a "tailored" tax situation, nevertheless agreed that fair relation is not a "narrow" concept, citing the relevance of general police and fire service. 453 U.S. at 647 (Blackmun, J., dissenting). The *Commonwealth Edison* dissent said that there is a limit: that interstate commerce not be unduly burdened by taxes that intentionally single out interstate business. The examples of such burdens given by the dissent have no relevance here, nor is there a claim of a tailored tax.

[29] *Commonwealth Edison* does state that the *measure* of the tax must be reasonably related to the extent of the contact, *i.e.*, "the activities or presence of the taxpayer in the State," but it explains that a tax measured as a percentage of the value of the taxed item provides the assurance that the tax is in "proper proportion" to the activities. 453 U.S. at 626. Since the Illinois tax is on Illinois purchases of telephone conversations with Illinois parties, and is measured as a percentage of those purchases, the distribution of tax burden "is assessed in proportion to a taxpayer's activities . . . in a State," so that "the taxpayer is shouldering its fair share of supporting" the State's benefits. *Id.* at 627.

shows, no benefit to the vendor is required—at least not where the taxpayer-purchaser receives benefits, in this case the vendor is very much present and operating in Illinois, both in general and in connection with the particular transaction being taxed, and therefore also benefits from the services and protection offered by the State.

Thus, on the fair relation test, as with the nexus test, this case presents an *a fortiori* situation compared to *Holmes*. Appellants' arguments (made before the *Holmes* decision) offer no possible rationale for abandoning the standards and logic of *Holmes* so soon after its unanimous issuance.

II. THERE IS NO REASON FOR THE COURT TO ACCEPT APPELLANTS' INVITATION TO RETREAT FROM THE CLARITY OF *HOLMES* INTO THE QUAGMIRE THAT PRECEDED IT.

Appellants advocate a course that would have the Court regress to the complexity, circularity, and confusion which members of the Court have seen in prior decisions on taxation of multi-state items and transactions—the "quagmire." *See Boston Stock Exchange v. State Tax Comm'n*, 429 U.S. 318, 329 (1977), citing *Northwestern States Portland Cement Co. v. Minnesota*, 358 U.S. 450, 458 (1959). Apart from the fact that the Court unanimously, clearly, and decisively took the path out of the quagmire in *Holmes*, and should not reverse course so soon for any reason, the course charted by appellants makes no sense.

A. The Court Should Not Revert To The Concept That Interstate Commerce Is Immune From State Taxation.

Appellants spend a great deal of effort revisiting the issue of the supposed dichotomy between a tax on the "privilege" of engaging in an interstate activity, and the purchase by an Illinois customer of a multi-state item. *See Spector Motor Service Inc. v. O'Connor*, 340 U.S. 602 (1951), overruled, *Complete Auto*, 430 U.S. at 289. The practical effect of their prescription for this case would

be to return to the semantic "formalism" of *Spector* and its principle "that a tax on the 'privilege' of engaging in an activity in the State may not be applied to an activity that is part of interstate commerce." *Complete Auto*, 430 U.S. at 278.[30]

The discussion in Part I above demonstrates why, if such semantic categorization were relevant, the tax here would fall on the "purchase" side. The distinction is substantially academic, however, since this Court has made clear that it will not let "the use of magic words or labels" "disable an otherwise constitutional levy." *Complete Auto*, 430 U.S. at 284, quoting *Railway Express Agency v. Virginia*, 355 U.S. 434, 441 (1959).

If the transactions at issue here, with quadruple layers of local nexus—the taxpayer, the activity, the transaction, and the vendor all have substantial local contacts—cannot be subjected to a percentage excise tax, very few such taxes involving interstate activity would pass muster, and the tax immunity principle of *Spector* would be revived.

Such a backslide would have to ignore the fact that in recent years "the Court has consistently indicated that 'interstate commerce may be made to pay its way,' and has moved to a standard of permissibility of state taxation based on its actual effect rather than its legal terminology." *Complete Auto*, 430 U.S. at 281. That progress culminated in the overruling of *Spector* in *Complete Auto* because "there was no real economic difference" between the taxes being sustained and those being invalidated under the *Spector* rule. *Id.* at 284. Appellants suggest no reason why this Court should revert to a rule "attaching constitutional significance to a semantic difference." *Id.* at 285. On the other hand, the States' vital interest in preserving and enhancing their ability to finance their

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[30] Indeed, appellants would have this Court go back 62 years before *Spector* to *Western Union Telegraph Co. v. Alabama State Bd. of Assessment*, 132 U.S. 472 (1889), to invalidate any tax which "was laid 'upon receipts properly appurtenant to interstate commerce,' and so constituted a tax on interstate activity." GTE Brief at 23, quoting *Western Union*, 132 U.S. at 476.

expanding role in the federal system and in not being excluded from access to the many new forms of information activities as a source of tax revenues, speaks loudly for confirming this Court's unanimous movement away from *Spector* and towards "permissibility" (*id.* at 281) of state taxation of transactions involving multi-state activities.

B. The Court Should Reject Appellants' Efforts To Transform An Uncomplicated Excise Tax On Activity With Ample State Nexus Into A Mandatory "Unitary Business/Formula Apportionment" Form Of Interstate Taxation.

Appellants' briefs disclose different views on what appellants really wish this Court to do here. GTE apparently would like this Court to rewrite all state taxes relating to interstate activity to conform to the "unitary business/formula apportionment" income tax model, a controversial and frequently litigated form of state taxation. Not only in its discussions of the *Complete Auto* "fairly apportioned" test, but in its discussions of the other three tests as well, GTE says that the result that it seeks is that "[a]ny state tax on interstate activity . . . must be limited to that portion of the interstate activity which occurs within the taxing State." GTE Brief at 11. While it cites *Complete Auto* for this proposition, no such language appears on the page cited or anywhere else in that decision. Rather, GTE's brief discloses that GTE reads into *Complete Auto's* use of the word "apportion" the entire burden of the "unitary business/formula apportionment" analysis set forth in *Container Corp. of America v. Franchise Tax Board*, 463 U.S. 159 (1983). See GTE Brief at 12, 25-26.

This Court, however, has consistently declined to mandate a particular form of taxing for the States. *See, e.g., Container Corp.*, 463 U.S. at 164; *Moorman Mfg. Co. v. Bair*, 437 U.S. 267, 280 (1978); *Northwestern States Portland Cement Co. v. Minnesota*, 358 U.S. 450, 462

(1959); *Wisconsin v. J.C. Penney Co.*, 311 U.S. 435, 444 (1940); *Henneford v. Silas Mason Co.*, 300 U.S. 577, 587 (1937).

Moreover, the particular model selected by GTE is totally inappropriate to the Illinois tax. As has been demonstrated above, the taxpayers, activities, transactions, and vendors subject to the Illinois tax all have "nexus aplenty" to the State imposing the excise tax. But the formula apportionment model of *Container Corp.* relates to state taxes on corporate net income from all transactions and activities involved in a corporation's "unitary" business, regardless of location or discernible nexus with the taxing State. It is the "formula" that provides an arithmetical estimate of the portion of this total income that can fairly be taxed by an individual State, *i.e.*, a "macro" estimate of nexus instead of a "micro" finding of nexus for each activity.

States choose the unitary form of tax because, in the context of a tax on a corporate income, ascertaining the State's nexus for each element of profit through "formal geographical or transactional accounting . . . is subject to manipulation and imprecision, and often ignores or captures inadequately the many subtle and largely unquantifiable transfers of value that take place among the components of a single enterprise." *Container Corp.*, 463 U.S. at 164-65. The State "instead calculates the local tax base by first defining the scope of the 'unitary business' of which the taxed enterprise's activities in the taxing jurisdiction form one part, and then apportioning the total income of that 'unitary business' between the taxing jurisdiction and the rest of the world on the basis of a formula taking into account objective measures of the corporation's activities within and without the jurisdiction." *Id.* at 165.

While the unitary income tax method is perfectly appropriate, valid, and constitutional,[31] it is not mandatory,

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[31] While not necessary to the decision here, since questions relating to the unitary tax are not involved in this case, it is in-

and cannot, under this Court's precedents, be made mandatory. The Illinois tax at issue here is neither a tax on net income nor a unitary tax, and thus the formula apportionment rules have no relevance.[32] Here, the es-

teresting to note that, as discussed in *Container Corp.*, the level of sales volume in a State is one of the valid apportionment formula factors (463 U.S. at 183-84), and the Court (divided as is usual on such issues) has allowed sales to be the single factor in an apportionment formula. *Moorman Mfg. Co. v. Bair*, 437 U.S. 267 (1978). The disagreement in the *Moorman* case related to whether the use of sales as the sole determinant for unitary taxation of an out-of-state business' entire profits "inevitably handicaps out-of-state businesses competing for sales in" the taxing State. *Id.* at 289 (Powell, J., dissenting). Justice Powell's dissent concluded that Iowa's formula "necessarily discriminates against out-of-state manufacturers" because among the other States with similar taxes there was "virtually universal use" of a three-factor formula, and the asymmetry automatically produced a disadvantage. *Id.* at 292. Among other reasons for upholding the tax, the majority saw no such inevitability because, even though Iowa's share of the sales was only 20%, the share of the profits generated by the Iowa sales might have been much greater, and, in fact, greater than the amount of profit actually taxed by Iowa. *Id.* at 276. Since there is no universal or even widespread conflicting formula here and no handicap whatsoever to out-of-state business, that dispute has no application to this case.

[32] The discussion in *Container Corp.* of the "internal" and "external" consistency requirements, on which GTE dwells, was in the context of taxation of a "unitary business' income." 463 U.S. at 169. Since then, the Court has extended the internal consistency requirement to gross receipts taxes (*Armco Inc. v. Hardesty*, 467 U.S. 638, 644-45 (1984), *Tyler Pipe Indus., Inc. v. Washington Dept. of Revenue*, 107 S.Ct. 2810, 2819-21, 2823 (1987)), and to flat taxes (*American Trucking Ass'ns, Inc. v. Scheiner*, 107 S.Ct. 2829, 2840 (1987)). The Illinois tax is perfectly internally consistent; if every State imposed a tax only on calls charged to customers in that State, no call would be taxed more than once. The Court has not expressly considered the external consistency requirement outside the *Container Corp.* context. In the context of sales taxes, the *Complete Auto* tests measuring nexus and fair relation ask essentially the same questions, and those tests are also satisfied in this case (see Parts I.A. and I.D., *supra*). In fact, because the entire concept of formula apportionment is a substitute for transaction-

sential fairness of the application of the State's taxing power is established by the nexus required for each separate taxed transaction. To repeat the conceded but vital facts, each call is to or from an Illinois telephone, purchased by an Illinois subscriber, and sold by a vendor offering its services to subscribers in Illinois and operating or purchasing transmission facilities in Illinois. Thus there is no need for a statistical proxy for the actual requirement of nexus in the Illinois statute.

C. This Court Should Not Impose A Mandatory "Slicing Of Shadows"[33] Requirement On State Taxation Of Telecommunications: Such A Requirement Is Not Constitutionally Required, Is Unworkable, And Is Inappropriate To The Activity Taxed.

The Goldberg variation on GTE's theme, probably recognizing its irrelevance, never mentions the *Container Corp.* discussion of formula apportionment. Instead, the Goldberg appellants would have this Court impose a requirement that "retailers bill consumers for the particular tax each participating State chooses to levy on its proportionate share of each communication." Goldberg Brief at 11. In other words, they would not allow a tax relating to interstate communications unless the electron stream were traced on its trip from point to point and some assessment made of the contribution by

by-transaction nexus, there is no reason to superimpose the external consistency test on the requirements of *Complete Auto*. But, in any event, a sales tax measured by the selling price has external consistency because it reflects the level of the taxpayer's economic activity and is not out of all proportion to services provided by the State. *Cf. Tyler Pipe*, 107 S.Ct. at 2822 ("selling tax measured by gross proceeds of sales is 'apportioned exactly to the activities taxed'") (quoting *Standard Pressed Steel Co. v. Washington Rev. Dept.*, 419 U.S. 560, 564 (1975)).

[33] *Container Corp.*, 463 U.S. at 192 ("Allocating income among various taxing jurisdictions bears some resemblance . . . to slicing a shadow").

each jurisdiction traversed in that trip. Other than citing different types of state taxes which avoid the issue (*id.* at 29)[34] they do not suggest how this task is to be accomplished, and as has been pointed out above (pp. 5-10), it would be a task of monumental, if not impossible, proportions. First, if this Court were to hold that such a tax was the only constitutional tax on interstate calls, each taxing State would have to place a tax on every call going out of, into, or "through" its territory to generate full revenue from this source. There would presumably have to be a menu of rates depending on the quantum and type of activity in the State: one rate for origination, one for wire transmission, another for microwave transmission, another for satellite sending and receiving, a different one for fiber optic cable, allocations for marketing and billing activities, operator assistance, and so on. Each of these rates would then have to be applied to the millions of calls travelling perhaps millions of routes every day.

Since even two "identical" calls may travel radically different routes through dozens of different States, using a variety of different facilities with different costs, each call would need its own multi-state tax bill. And since the routing can change in the middle of a single call as well, some calls might have more than one tax calculation. While GTE claims that it can bill for two taxes on one call (a claim placed in doubt by its inability in this case to succeed in billing for even one tax (see n.21, *supra*)), it does not claim that it can bill for dozens of different taxes on each call, nor is there any evidence

[34] The Goldberg Brief asks (at 29) that "States recognize that *some* apportionment efforts must be made." Of course, Illinois *de facto* does so: it does not levy its tax on many calls with an Illinois nexus, such as calls into the State that are charged to a customer in another State. Thus, if the entire universe of calls to and from Illinois were aggregated, and assuming that half (by value) are charged to Illinois customers and half are not, then the levy is, overall, on 50% of the value of all such calls.

that it or any other interstate carrier would want to do so. Nor is the customer likely to want to receive a bill with dozens of state taxes itemized on each call, with no way to comprehend their source or assess their validity.

In fact, taxpayers are likely to wonder what their would-be class representatives have gained for them in the process. In all likelihood the total cost to the taxpayer would be at least as great as the single state tax at issue in this case, since, if the system were practicable, most States would want to join in; and every segment of every call would be taxed at full value. Moreover, the tremendous cost of all the required bookkeeping and billing would also be passed on to the customer (and by increasing the costs of the calls would also increase the tax).

Before reaching the question whether such a nightmare is constitutionally required, one may ask, where is the benefit to taxpayer or vendor? Right now the Illinois customer who buys a long distance call to a cousin in New York by dialing direct or by accepting the charges on a collect call, or by using a credit card, pays one tax to Illinois of 5% of the cost of the call. If New York has the same type of tax, the cousin will pay it on every call made to Illinois and charged to his New York number. Appellants suggest no way that either one of them is better off by paying, say, 2% to his own State, 2% to the distant State, and 1% divided up among five or ten other States, especially if the calls cost more as a result, and the bills need a page for each call.[35]

[35] It should be noted that under the Goldberg appellants' theory, a similar system might have to be imposed for many long distance calls between points in the same State that are routed via out-of-state switching centers or go via satellite, perhaps through out-of-state ground stations. Thus a call from one point in Maine to another might have to be billed for both Maine and New Hampshire taxes. See n.11, *supra*.

In fact, what the Goldberg appellants are suggesting is not only unworkable, it adds nothing to the fairness or equity of the situation for any of the parties to long distance calls. While increased fairness is not a sufficient condition for invoking the Commerce Clause to invalidate a state tax, it certainly is a necessary condition: the whole thrust of the *Complete Auto* tests is to improve the fairness of the tax system to those who bear its burdens. Appellants cannot meet that threshold barrier to their plea to this Court.

CONCLUSION

For the reasons stated, the judgment of the Illinois Supreme Court should be affirmed.

Respectfully submitted,

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June 22, 1988

Nos. 87-826, 87-1101

In The Supreme Court of the United States

October Term, 1987

JEROME F. GOLDBERG and ROBERT McTIGUE,
Appellants,

v.

ROGER D. SWEET,
DIRECTOR OF THE ILLINOIS
DEPARTMENT OF REVENUE, *et al.*,
Appellees.

GTE SPRINT COMMUNICATIONS CORPORATION,
Appellant,

v.

ROGER D. SWEET,
DIRECTOR OF THE ILLINOIS
DEPARTMENT OF REVENUE, *et al.*,
Appellees.

On Appeal From The Supreme Court Of Illinois

MOTION FOR LEAVE TO FILE BRIEF AND BRIEF OF AMICUS CURIAE MCI TELECOMMUNICATIONS CORPORATION IN SUPPORT OF AFFIRMANCE

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41 PV

MOTION OF AMICUS CURIAE MCI TELECOMMUNICATIONS CORPORATION FOR LEAVE TO FILE BRIEF IN SUPPORT OF AFFIRMANCE

Pursuant to Supreme Court Rule 36.3, MCI Telecommunications Corporation ("MCI") moves for leave to file the accompanying brief as *amicus curiae* in support of affirmance.

MCI Telecommunications Corporation owns and operates the world's second largest communications network. MCI's long distance offerings permit customers to call every telephone in the United States and in 146 foreign countries. MCI provides communications employing state of the art fiber-optic cable, digital microwave, and satellite communications technologies. Currently, MCI is subject to a multiplicity of taxes on various types of intrastate and interstate calls.

MCI has three distinct interests affected by this case. First, and most obviously, it has an interest in minimizing the tax burden on its customers by eliminating any multiple taxation of telecommunications. Second, it has an interest in minimizing the costs to itself and its customers of administering and complying with State taxes by promoting forms of taxation which are easy to administer and comply with. MCI believes that the Illinois telecommunications tax represents a form of taxation which most efficiently reduces the risk of multiple taxation while minimizing administrative burdens. Thus, the Illinois tax is the least objectionable type of tax on telecommunications and MCI has an interest in having its constitutionality upheld.

Third, MCI has an interest in the reduction of the currently prevailing uncertainty of the constitutional standards in this area, which will minimize future litigation and allow governments to select the least onerous of the permissible methods of taxation. MCI believes that the wide variations in the forms of taxation now imposed by State and local governments result in part from uncertainty as to what forms of taxation are constitutionally permissible. The very variety of disparate taxes with which MCI must deal imposes additional burdens upon it.

Moreover, during the pendency of litigation such as this, injunctions are sometimes issued requiring MCI to maintain extensive records, not otherwise necessary to its business, in order to facilitate distribution of refunds among its customers should the tax be found invalid. All of these burdens would be ameliorated by greater certainty as to the constitutional standards. Finally, MCI may be compelled to incur substantial administrative costs if a refund is necessary in this and other cases.

MCI was named as a party in the courts below. This makes MCI a party under Rule 10(4) of the Court, inasmuch as the Rules do not differentiate between named, active, nominal or financially interested parties. MCI's role in the case is that of a named party who is absorbing a substantial and costly administrative burden in acting as a conduit for collection and transmission of the tax from its customers to the State of Illinois. MCI filed an answer and a counterclaim in the trial court in order to take advantage of a statutorially created escrow fund with the Treasurer of the State of Illinois in the event the tax is found invalid and a refund is necessary. Finally, MCI may be involved administratively in the event a refund is necessary.

While MCI's direct interest in this case, as a cross-claiming defendant, tends to be aligned with those of appellants, MCI is nevertheless supporting the position of appellees in order to advance its customers' and its own broader interests in eliminating multiple taxation while minimizing the burdens of administering and complying with State and local taxation. Therefore, MCI believes that it is more appropriate that it participate in this case as an *amicus curiae* rather than as a party.

MCI believes that it is important that application of established legal standards to this case be enlightened by an understanding of the practicalities of the telecommunications business in which MCI is engaged. Appellants have failed to address important practical aspects of that business and have made statements about other aspects which appear susceptible to misunderstanding. Appellees, officials of the State of Illinois, are not fully conversant with these practicalities and are therefore not able

to address them as fully as MCI. Moreover, MCI wishes to present certain arguments regarding the legal significance of these practical realities and of the economic impact of the tax which the State of Illinois has not presented or has presented less fully than MCI believes they deserve.

MCI has sought the consent of counsel for appellants and counsel for appellees for leave to file the accompanying brief. Counsel for appellant GTE Sprint Communications Corporation denied this request.

For the foregoing reasons, MCI prays that the Court grant its request for leave to file the accompanying brief.

Respectfully submitted,

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On Appeal From The Supreme Court Of Illinois

BRIEF OF AMICUS CURIAE MCI TELECOMMUNICATIONS CORPORATION IN SUPPORT OF AFFIRMANCE

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QUESTION PRESENTED

Where a State imposes a tax of 5% of the purchase price on purchases of all telephone calls originating or terminating in the State and charged to telephones located in the State, is the State constitutionally required to attempt to apportion the charges for individual interstate phone calls between charges for in-state facilities and those for out-of-state facilities even though:

(1) the unapportioned tax on the purchasers of the calls is economically equivalent to a validly apportioned gross receipts tax on the seller of the calls;

(2) there is no evidence that there is any practicable way to make a meaningful apportionment of charges for individual phone calls among the States involved in transmitting those calls;

(3) each interstate telecommunication would be taxed only once if the same tax were adopted by every State;

(4) the tax provides a credit for any taxes imposed on the purchase of the same call by any other jurisdiction;

(5) the tax is imposed equally on purchases of intrastate and interstate phone calls; and

(6) the tax is reasonably related to services rendered by the State to the purchaser of the calls?

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STATEMENT OF THE CASE

Because established commerce clause principles must be applied in light of the technological realities of modern telecommunications, the structure of interstate telecommunications networks will be addressed before describing the tax at issue.

Interstate Telecommunication Networks

A number of carriers compete with one another in the interstate telecommunications market. These include MCI, appellant GTE Sprint Communications Corporation ("GTE Sprint"), and all of the other carriers named as defendants in this case except Illinois Bell Telephone Company.[1] Each of them, like GTE Sprint, has "established over the years and at great expense, its own interstate transmission network comprised of microwave radio, fiber optic, satellite and cable facilities, spread over numerous states." (GTE Sprint Br. 3.) Of course, it is self-evident that the actual satellites involved in these networks are in outer space, beyond the territory of any State.

As telecommunications are placed by customers and enter such a network, they are routed by computers which attempt to maintain optimal use of all of the various facilities in the network. The routing selected for a given call depends on the usage of the network when the telecommunication is received, so that various communications between the same two points may utilize many different routings. Thus, one telecommunication from Chicago to New York might proceed by a ground circuit directly connecting the two cities and passing through Indiana, Ohio, Pennsylvania, and, perhaps, New Jersey. If such direct circuits are all busy or otherwise unavailable, another telecommunication may be routed, in part, through Michigan, Wisconsin, Canada, or any of a virtually infinite variety of less direct, but available, circuits. Alternatively, the telecommunication might be transmitted directly from Illinois to New York via satellite,

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[1] Illinois Bell is a local exchange carrier which does not itself provide interstate telecommunications service, although it does provide "access" connections between its own customers and interstate carriers.

without passing through any State other than the States of origination (Illinois) and termination (New York).

The number of telecommunications which must be routed is staggering. During 1987, MCI alone was carrying an average of 6,901 long distance telecommunications per minute for each minute of a 24-hour day. The industry as a whole was carrying over 69,000 such telecommunications per minute.

MCI has no existing means of determining how any particular prior communication was routed or of routinely recording the routing of a current communication. So far as MCI is aware, no other carrier has the ability to make such determinations or records. Thus, MCI believes that it is literally impossible at the present time to meaningfully apportion the charge for a particular call among the States through which that call was transmitted, for there is no way to ascertain the identities of those States. Moreover, the very number of calls involved demonstrates that, even if it were technically feasible to record and analyze routinely the routing of every call, the time, equipment, and expense involved for the carriers would be enormous.

Surely nothing in this record even suggests that such call-by-call apportionment would be even theoretically possible, let alone practically feasible. To the extent that appellants assert otherwise,[2] the record simply fails to support that assertion. Appellants' sole reliance in this regard is on a single paragraph in an affidavit submitted by one of GTE Sprint's attorneys, Richard Wiley:

> GTE Sprint has the administrative capability to bill taxes to its customers on telecommunications services which originate in any state, or terminate in any state, or are billed in any state, or any combination of these criteria for any number of states. Specifically, GTE Sprint has the administrative capability to bill more than one state's tax to a single customer for a single communication. For example, GTE Sprint can bill an Illinois customer for an interstate telecommunication originating in Illinois and terminating in New York, and could include, in that charge, a tax assessed by Illinois, the originating state, and New York, the terminating state.

(GTE Sprint J.S. App. 9a.)

All that this paragraph actually says is that GTE Sprint, like MCI and other carriers, could put line items on its bill for as many State taxes as might be applicable. It does not say, or even suggest, that GTE Sprint could apportion the charges for individual calls among the States (or even identify the relevant States), for purposes of computing such taxes, on any basis reflecting the actual routings of those calls. Indeed, nowhere in their briefs do any of the appellants suggest any method of apportioning the charges for individual calls other than purely arbitrary formulas. As a result, MCI believes that a constitutional requirement for the sort of apportionment appellants appear to demand would render it impossible for any State to impose a meaningful tax on purchases of interstate telecommunications.

The Illinois Telecommunications Excise Tax

Illinois imposes a tax upon retail purchasers of both intrastate and interstate telecommunications. Telecommunications Excise Tax Act ("Act"), §§3-4, Ill. Rev.Stat. ch. 120, ¶¶ 2003-04 (reprinted as Appendix F to the Jurisdictional Statement of Goldberg ("Goldberg, J.S.)) The seller of the telecommunication service is obliged to collect the tax from the purchaser by adding the tax to the charge billed to the purchaser and to remit the tax to the State. Act, § 5.[3]

[2] Appellants Goldberg and McTigue (collectively, "Goldberg") assert that "carriers now have the capability to bill each telephone customer for whatever tax each participating State chooses to levy on its proportionate share of each call charged to the customer's account." (Goldberg Br. 30 n.24.) GTE Sprint asserts that it is capable of billing "any tax assessed by any one state on the call's transmission path." (GTE Sprint Br. 4.)

[3] As is customary for sales taxes, a seller which fails to collect the tax is made liable for the amount not collected. Act, § 5. This provision is the basis for the payment by GTE Sprint of $400,000 of its own funds for calls where it fails to collect the tax. (GTE Sprint Br. 9.)

No tax is imposed on an interstate telecommunication unless the telecommunication purchased is either originated or received in Illinois. Act, § 4. Regardless of whether the telecommunication is intrastate or interstate, the tax is "5% of the gross charge for such telecommunication" made by the retailer from whom it is purchased. *Id.* The "gross charge" on which the tax must be paid means the "amount paid" for the telecommunication, subject to certain statutory exclusions.[4]

The "amount paid" is defined to be the amount "charged to the taxpayer's service address in this State." Act, § 2(b). By customary usage in the industry, a "service address" is the location of a telephone or other telecommunications device and is not necessarily the same as the address to which the bill is sent. For example, an individual with a telephone at his vacation home (the service address) might have the bills for that telephone sent to his primary residence (the billing address). Similarly, a corporation with many offices might have the phone bills for all of them sent to its headquarters. For purposes of the Illinois tax, only the location of the service address is significant, so it does not matter where the bills are sent or where they are paid. That is, a call originating or terminating in Illinois is taxable if and only if it is "charged to a service address in [Illinois], regardless of where [it] is billed or paid."[5] Act, § 2(b).

In the normal course of events, a telecommunication is "charged" to the telephone or other device from which the purchaser originates the communication, and the location of that device is the relevant service address. For collect communica-

[4] Section 2(a) of the Act defines "gross charge" and specifically excludes amounts billed to the purchaser for (1) certain other taxes, (2) charges for certain collect telecommunications, (3) charges for certain data processing services, and (4) charges for customer equipment.

[5] While some loose language in the Illinois Supreme Court's Opinion (Goldberg J.S. App. 10a, 11a) suggests that the place of billing or payment might be significant, the statute expressly provides otherwise and the parties all recognize this. (Goldberg Br. 3; GTE Sprint Br. 5, 14, 19, 29; Consolidated Mo. to Affirm 5-6 & n.4.)

tions, the charge is made to the service address at which the purchaser receives the communication. By use of a credit card or similar arrangement, a purchaser can arrange to have a call charged to a service address other than those where the call is originated or received. But for any taxable communication, the purchaser must both have an Illinois service address and in some way cause the communication to be charged to a telecommunications device at that address. Otherwise, there will be no "amount paid" to be subjected to the Illinois tax, even when an interstate call originates or terminates in Illinois.

Thus, Illinois has not attempted to tax any telecommunications which merely pass through Illinois on their way between other States. Nor has it attempted to tax interstate calls originating or terminating in Illinois if they are charged to telephones located elsewhere. Illinois has not even attempted to tax telecommunications charged to Illinois telephones unless those telecommunications either originate or are received in Illinois.

Moreover, with respect to interstate telecommunications, the Act provides a credit to further protect against multi-state taxation of the same taxable event. Any taxpayer who pays taxes in both Illinois and another State on the same call may claim a credit against the Illinois tax in the "amount of such tax properly due and paid in such other state." Act, § 4.

Procedure Posture

The procedural history of this case is adequately addressed in the briefs of the parties. The interest of *amicus curiae* is set forth in MCI's motion for leave to file this brief. The reasoning of the trial court in holding the tax invalid and of the Illinois Supreme Court in reversing and upholding the tax will not be set forth in this brief because MCI does not rely upon or endorse that reasoning. However, the Court reviews judgments, not opinions, and must affirm the judgment if it is correct, even if the reasons why it is correct are different from those advanced by the courts below. *Chevron, U.S.A., Inc. v. Natural Resources Defense Council*, 467 U.S. 837, 842 & nn. 7-8 (1984). For the reasons stated

herein, MCI believes that the judgment of the Illinois Supreme Court was correct.

SUMMARY OF ARGUMENT

A proper decision in this case involves application of well-settled Commerce Clause jurisprudence to the scientific advancements of the third century of our nation's and its Constitution's existence. The issue before the Court arises in the context of a monumental change in technology. Transmission of messages from point A to point B is no longer accomplished solely by electric impulses over identifiable telephone lines. Rather, such transmissions now utilize computer selected routings for each telecommunication over ever-changing sets of circuits within a vast interconnected network. The routing of two consecutive communications between the same two points may be entirely different and there is no means in existence of recording how any particular communication is transmitted. Moreover, many communications are transmitted via satellites beyond the boundaries of any State. For these reasons, it is impossible for MCI – and, so far as MCI is aware, for any other carrier – to "identify that percentage of instate transmission activity and costs involved in each long distance call, and confine the Illinois tax to the corresponding percentage of the call's gross charge." (GTE Sprint Br. 31.) Appellants' suggestions that individual telecommunications be mathematically apportioned ignore both these technological realities and the Commerce Clause principles laid down by this Court.

The linchpin of appellants' argument is that the Illinois tax violates the Commerce Clause because it taxes the entire amount of each interstate telecommunication charged to an Illinois service address, rather than providing for a mathematical apportionment of the charge based on the proportionate involvement of Illinois facilities in delivering the telecommunication. Appellants claim that failure to apportion the tax mathematically: (i) creates a risk of multiple taxation of the same telecommunication by different States, (ii) causes the tax to discriminate

against interstate commerce, and (iii) eliminates any fair relation between the tax and the services provided by Illinois.

While the Illinois tax does not attempt to apportion the charges for the individual calls taxed, it carefully limits the scope of the tax imposed to provide the functional equivalent of apportionment. For Commerce Clause purposes, what matters is not the form of the tax, but its economic effect. While the tax here is a sales tax imposed on the purchaser of the call, the burden on commerce imposed by such a tax is economically equivalent to that imposed by a gross receipts tax on the seller of the call. The seller, of course, has gross receipts from many sources, but the tax would only apply to receipts from calls sold to Illinois service addresses. Thus, from the seller's perspective, the tax effectively would be a tax on all gross receipts with an apportionment among jurisdictions based on sales, and the Court has held that a gross receipts tax apportioned in that way is permissible under the Commerce Clause. Because the economic effect of the Illinois tax on interstate commerce is equivalent to the effect of a validly apportioned gross receipts tax, and because it is the economic effect which determines the validity of the tax, the Illinois tax is also valid.

This conclusion is reinforced by what MCI believes to be insurmountable administrative and technological barriers to meaningful mathematical apportionment. Because of the impracticability of determining the paths taken by individual calls and the vast differences in the level of State involvement among the various different modes of transmission utilized by modern networks, the modern, high technology realities of telecommunications do not permit the paths over which telephone messages are transmitted to be analogized to the relatively fixed (and readily determined) routes over which trucks or buses operate in a relatively uniform fashion. Thus, the rules for taxation of, for example, interstate motor carriers – whose approximate mileage in each State can be tallied and reported and whose mileage in one State is qualitatively similar to that in another – are not workable or appropriate for the minute-by-

minute taxation of interstate telephone calls whose individual routings through particular States, or in space outside the territory of any State, cannot practicably be traced or recorded and utilize a variety of dissimilar transmission methods with varying connections to individual States.

In contrast, it is administratively simple to allocate each call to the service address where it is charged and to compute the tax imposed at that location. Moreover, such an allocation limits the taxing State to only its fair share of the total telecommunications activity affecting it, so that the enormous expense and effort necessary even to attempt apportionment of individual calls would serve no purpose in fairly distributing taxing power among the States.

What is striking about the Illinois tax is that it achieves the objectives of Commerce Clause restrictions on State taxation, even though it does not provide for apportionment of individual calls. The Illinois scheme is designed both to avoid multiple taxation of the same telecommunication and to tax only a fair share of all the telecommunications activity conducted in or affecting Illinois. The tax is imposed only upon calls which an Illinois taxpayer elects to have charged to his service address in Illinois and thus fairly measures the protection and services Illinois provides to the taxpayer and the telecommunications equipment located at that address. For this reason, MCI submits that the Commerce Clause validity of the tax should be upheld as a meaningful adaptation of legislative methodology to technological innovation.

ARGUMENT

I. A STATE SHOULD BE PERMITTED TO TAX PURCHASERS OF INTERSTATE TELECOMMUNICATIONS BY ALLOCATING PARTICULAR CALLS ENTIRELY TO ITSELF SO LONG AS THE ALLOCATION METHOD IS ECONOMICALLY EQUIVALENT TO A VALID METHOD OF APPORTIONING A GROSS RECEIPTS TAX IMPOSED ON THE SELLER.

Since the Court's decision in *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274 (1977), it has been clear that the validity under the Commerce Clause of a State tax does not depend on its form, but rather on its "practical effect" based on "economic realities." *Id.* at 279; *Westinghouse Electric Corp. v. Tully*, 466 U.S. 388, 404 (1984) (validity must be judged by "economic effect" of tax). Thus, the issue is "whether the tax produces a forbidden effect," such as preferring local business or subjecting interstate commerce to multiple, cumulative burdens of a sort not faced by local business. *Complete Auto Transit*, 430 U.S. at 288.

A. The Illinois Telecommunications Tax Is Economically Equivalent To a Gross Receipts Tax on Sale of Telecommunications to an Illinois Service Address.

The Illinois telecommunications tax is, both in form and in substance a sales tax imposed on the purchaser of the telecommunication. In terms of the burdens imposed on interstate commerce, such taxes are economically equivalent to gross receipts taxes imposed on the seller.

If the seller charges $1 for a particular telecommunication, the Act requires it to add a tax of five cents and collect $1.05 from the purchaser. To the extent that the increased cost to the purchaser results in reduced demand for telecommunications, the seller will be required to either accept the reduction in volume or reduce the charge for the telecommunication to fully or partially offset the effect of the tax. However, because all competing sellers of telecommunications are faced with the same tax, it does not alter their relative competitive positions, so any reduction

in volume will come only from communications either foregone entirely or diverted to slower methods such as the mails.

If a seller were instead faced with imposition of a gross receipts tax, maintenance of the seller's prior untaxed revenues from a call formerly costing $1.00 would require raising the price to a level which would net out to $1.00 after payment of the tax.[6] If the resulting price were $1.05, purchasers would be expected to react to such a price increase in exactly the same way they would react to an effective increase resulting from the addition of a five cent tax to a $1.00 selling price. Because the gross receipts tax represents a cost resulting specifically from the sale generating the receipts, it must be recovered by increasing the price of that sale or absorbed as an overhead item taking the form of reduced net receipts from that sale. Thus, the seller faces exactly the same choice (accepting reduced volume or absorbing part of the tax to limit the amount of the price increase) presented by imposition of a sales tax. Moreover, because all competitors are again faced with the same tax, the economic incentives will be the same in both situations.

Thus, both buyers and sellers should behave identically regardless of which form the tax takes. Accordingly, the "practical effect" on interstate commerce should likewise be identical, regardless of whether the tax takes the form of a sales tax or a gross receipts tax. *See, e.g.*, P. Samuelson and W. Nordhaus, *Economics* 387-89 and n.5 (12th Ed. 1985); *Gurley v. Rhoden*, 421 U.S. 200, 204 (1975).

[6] To be precisely equivalent to a 5% sales tax, the gross receipts tax would have to require raising the price to $1.05. Because the tax base for a gross receipts tax includes the tax, while a sales tax is an addition to the seller's net price, the rate would differ slightly. Thus, the gross receipts tax rate equivalent to a 5% sales tax would be five cents on receipts of $1.05, a rate of roughly 4.76%. For any given sales tax rate, it is possible to compute an equivalent gross receipts tax rate.

B. The Court's Decisions Expressly Permit Gross Receipts Taxes To Be Apportioned on the Basis of the Location of the Delivery of the Purchase.

Had the Illinois telecommunications tax taken the form of a gross receipts tax on the revenues derived by the sellers from the same calls as are subject to the present sales tax, it would have presented a situation virtually identical to those considered by the Court in *General Motors Corp. v. Washington*, 377 U.S. 436 (1964), *Standard Pressed Steel Co. v. Washington Department of Revenue*, 419 U.S. 560 (1975), and in the portion of *Tyler Pipe Industries, Inc. v. Washington State Department of Revenue*, 107 S. Ct. 2810 (1987), dealing with out-of-state sellers challenging the tax on in-state sales.[7]

In *General Motors* and *Standard Pressed Steel*, the Court rejected challenges by out-of-state sellers to a Washington tax on the unapportioned gross receipts from sales of goods delivered in Washington, even though the sales resulted from manufacturing and distribution activities which predominantly occurred in other States. In *General Motors*, the Court noted that taxes measured by gross receipts from interstate commerce must be carefully scrutinized to guard against "the danger that such taxes can impose cumulative burdens upon interstate transactions which are not presented to local commerce." *Id.* at 440. "Nevertheless, . . . it is well established that taxation measured by gross receipts is constitutionally proper if it is fairly apportioned." *Id.*

The standard to be applied in determining whether a State tax is fairly apportioned was more fully summarized in *General Motors*:

> A careful analysis of the cases in this field teaches that the validity of the tax rests upon whether the State is exacting a constitutionally fair demand for that

[7] *Tyler Pipe* did invalidate the application of the Washington tax to in-state manufacturers selling in other States and, in so doing, partially overruled *General Motors*. However, as explained at 12-13, *infra*, that aspect of *General Motors* is not relevant to the problem here, and *Standard Pressed Steel* was relied upon and fully reaffirmed.

aspect of interstate commerce to which it bears a special relation.... In other words, the question is whether the State has exerted its power in proper proportion to appellant's activities within the State and to appellant's consequent enjoyment of the opportunities and protections which the State has afforded.... As was said in Wisconsin v. J.C. Penney Co., 311 U.S. 435, 444 (1940), "[t]he simple but controlling question is whether the state has given anything for which it can ask return."

Id. at 440-41. *Accord Standard Pressed Steel*, 419 U.S. at 562.

Despite the fact that the tax was nominally "unapportioned and ... therefore suspect," *General Motors*, 377 U.S. at 448, it was nonetheless upheld as applied to sales made to Washington customers. As applied to such sales, the Court found that the tax was "'apportioned exactly to the activities taxed,' all of which are intrastate." *Standard Pressed Steel*, 419 U.S. at 564. The Court distinguished *Gwin, White & Prince, Inc. v. Henneford*, 305 U.S. 434 (1939), where it had forbidden application of a similar Washington tax to sales made by Washington businesses and shipped to customers in other States. In the latter situation, the Court perceived a danger that the buyer's State would also impose an unapportioned sales or gross receipts tax, thereby subjecting interstate commerce to "the risk of a multiple burden to which local commerce is not exposed." 419 U.S. at 564.

The lesson of these cases is that restricting a gross receipts tax to receipts from sales made to customers in the taxing State is sufficient to constitute a fair apportionment of that tax. The Court later reaffirmed that rule and relied on it as a basis for holding that a State may validly apportion a net income tax solely on the basis of the taxpayer's sales in the various States from which it derives revenue. *Moorman Manufacturing Co. v. Bair*, 437 U.S. 267, 280-81 (1978)

The portion of these cases pertinent here was carefully reconsidered and reaffirmed only a year ago in *Tyler Pipe Industries, Inc. v. Washington State Department of Revenue*, 107 S. Ct. 2810 (1987), although *General Motors* was overruled on another

point.[8] The Washington tax was imposed as a single tax on the act or privilege of engaging in business in Washington. Among the taxable activities were both manufacturing and selling in Washington. The tax was a percentage of sales arising from the Washington activity. The tax was challenged by both out-of-state manufacturers selling in Washington and Washington manufacturers selling out-of-state, both of which claimed to suffer discrimination in comparison with Washington manufacturers who sold in that State.

The source of the alleged discrimination was the fact that companies both manufacturing and selling in Washington were subject to only the single tax on their receipts, while companies manufacturing in one State and selling in the other were subject to both the Washington tax on their revenues and whatever tax was imposed by the other State on the activities conducted there. As to those manufacturing in Washington, and selling elsewhere, this Court found the tax invalid because it failed the test of "internal consistency" under which "'the [tax] must be such that, if applied by every jurisdiction, there would be no impermissible interference with free trade.'" 107 S. Ct. at 2816, *quoting Armco, Inc. v. Hardesty*, 467 U.S. 638, 644 (1984). (That test is discussed at 21-24, *infra*.) Thus, as in *Gwin, White & Prince*, this Court forbade application of the tax to sales made by Washington manufacturers for delivery in other States. Because all of the sales here are made to an Illinois service address, that aspect of the case is not relevant here.

However, as to out-of-state manufacturers selling in Washington, this Court again upheld the tax. 107 S. Ct. at 2821-22. In particular the Court squarely rejected the claim that a tax imposed on in-state sales was not fairly apportioned because the sales were the culmination of multi-state activity in manufacturing and distribution. Relying on *Standard Pressed Steel* and *Moorman Manufacturing Co.*, the Court reasoned that "whole-

[8] Some aspects of the analysis in *General Motors* were also disapproved, but this did not affect the result on the present issue.

saling – whether by an in-state or an out-of-state manufacturer – must be viewed as a separate activity [from the prior manufacturing and distribution] conducted wholly within Washington that no other State has jurisdiction to tax." *Id.* at 2822. Thus, *Tyler Pipe*, like the prior cases, held that a gross receipts tax may be imposed on all sales made for delivery in the taxing state but not on sales made from the taxing state for delivery elsewhere.

This result is eminently sound. It is generally recognized that the economic burden of either a sales tax or a gross receipts tax falls primarily on the purchaser of the goods or services sold. *See, e.g., Gurley v. Rhoden*, 421 U.S. 200, 204 (1975). Structuring such taxes so that they fall on purchasers in the taxing State serves a major purpose of the Commerce Clause: preventing exploitation of interstate commerce to shift tax burdens onto out-of-state interests powerless to participate in the local political process. *See, e.g., McGoldrick v. Berwind-White Coal Mining Co.*, 309 U.S. 33, 45-46 n.2 (1940).[9] Moreover, such structuring fairly divides the tax base represented by sales among the States: each may tax the portion represented by purchases in its own territory. Were such taxes based on the location from which the goods were sold, as in *Gwin, White & Prince* and one portion of *Tyler Pipe*, then States which were net exporters would receive a disproportionate share of the revenue while a disproportionate share of the burden would fall in States which were net importers. Finally, structuring sales and gross receipts taxes on the basis of the location of the purchase is easily administrable and requires no complex accounting for individual transactions.

[9] As explained in *McGoldrick*, Commerce Clause jurisprudence is largely based on "the recognized danger that, to the extent the burden falls on economic interests without the state, it is not likely to be alleviated by those political restraints which are normally exerted on legislation where it affects adversely interests within the state." 309 U.S. at 45-46 n.2.

Taxation of interstate telecommunications based on the location of the telephone or other device to which they are charged is closely analogous to taxation of ordinary sales based on the location. That location provides a unique nexus which fairly reflects the role of each State as a consumer of telecommunications.[10] It assures that a purchaser with a local presence, and an ability to participate in the local political process, will bear the burden of the tax. Finally, it provides the simplest mechanism administratively for division of this tax base among the States.

Thus, the Illinois tax is based on an allocation method (location of sales) which this Court has recognized as a permissible basis for apportionment of a gross receipts tax on interstate commerce. The Illinois tax is economically equivalent to such a permissible tax and the same reasoning shows that it fairly and simply divides the tax base among the States and prevents the shifting of tax burdens to the residents of other States. Thus, judging the Illinois tax by its "practical effects" and in light of "economic realities," that tax too should be found permissible under the Commerce Clause.[11]

[10] Insofar as some States may contribute to maintenance of interstate telecommunications networks to a greater extent than they consume the services of those networks, those contributions can be recognized through property taxes on telecommunications facilities, employment taxes on telecommunications personnel, or any of a variety of taxes based on the activities occurring in those States. The recognition in *Tyler Pipe* that out-of-state manufacture and distribution are separate from in-state sales for Commerce Clause purposes confirms that such taxes on the activities involved in maintaining interstate networks may be imposed without affecting any tax on the ultimate sale. Therefore, contrary to the implications of appellants' demand for apportionment in accordance with the respective facilities which each State contributes to a given call, disproportionate contributions to the telecommunications network ought not to be the basis for awarding States a constitutional entitlement to a disproportionate share of the revenues derived from consumption of telecommunications.

[11] In challenging the propriety of using the location of the service address as an apportionment mechanism, GTE Sprint relies (GTE Sprint

(Footnote continued on the following page)

II. WHERE A STATE IMPOSES A TAX ON PURCHASERS OF INTERSTATE TELECOMMUNICATIONS, ITS FAILURE TO ATTEMPT TO APPORTION THE CHARGES FOR INDIVIDUAL CALLS DOES NOT RENDER THE TAX INVALID WHERE THERE HAS BEEN NO SHOWING THAT MEANINGFUL APPORTIONMENT OF INDIVIDUAL CALLS IS PRACTICABLE AND THE STATE HAS TAKEN REASONABLE STEPS TO AVOID TAXING MORE THAN ITS FAIR SHARE OF INTERSTATE TELECOMMUNICATIONS ACTIVITY.

A. Apportionment Is Not Required Unless It Is Shown To Be Practicable.

GTE Sprint argues that a tax on telecommunications must be apportioned according to "that portion of Illinois transmission activity and costs involved in a long distance call, while protecting substantial non-Illinois transmission activity and costs from taxation." (GTE Sprint Br. 30.) For the reasons discussed above, it is virtually impossible to devise an apportionment formula that fairly reflects the involvement of each State affected by every individual interstate telephone call. The technological reality is that calls are transmitted by different modalities (satellite, microwave, fiber-optic cable etc.), some of which require the use of physical facilities in some or all of the States traversed and others of which do not involve significant contribution by the States whose paths are crossed by the telecommunication.

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11 *(Continued)*

Br. 29-31) on the requirement of "external consistency" imposed on State methods of apportioning the net income realized by a taxpayer from activities throughout the nation. *See Container Corp. of America v. Franchise Tax Board*, 463 U.S. 159, 169 (1983). It is unclear whether or how this requirement might apply to taxes on something other than net income (for which some sort of largely artificial apportionment mechanism is inherently necessary to divide an indivisible quantity among multiple jurisdictions). However, if that requirement does apply to sales taxes or equivalent gross receipts taxes, the cases just discussed necessarily establish that apportionment by the volume of sales made to the taxing State satisfies that requirement.

See generally, W.J. Blyth and M. Blyth, *Telecommunications: Concepts, Development, and Management* 85-113 (1985). Thus, for example, the path of a microwave communication may pass through a State between microwave relays in adjacent States without utilizing any actual facilities in the intermediate State. Other communications bypass any intermediate States by use of satellites outside the territory of any State, so that any allocation of that contribution among States would, of necessity, be purely arbitrary. The upshot is that even if one could determine the path of every telecommunication, an apportionment of the charge based on the distance traveled within each State would have only a minimal relation to the respective amount of activity involved in each of those States. *See Pan American World Airways, Inc. v. Virgin Islands*, 459 F.2d 387, 393-95 (3rd Cir. 1972)(making similar point regarding air travel). In sum, there is no way to apportion a single telecommunication meaningfully according to the involvement of States touched by a transmission.

The inappropriateness of requiring mathematical apportionment of individual telephone calls is underscored by the extreme practical obstacles to keeping track of the routes of the millions of calls transmitted yearly. As explained above, MCI has no existing means by which it could determine how any particular prior communication was routed or of recording the routing of a current communication and MCI does not believe that any other carrier has the ability to make such determinations or records. Yet, without such records, it is impossible even to determine which States (other than those of origin and destination) were involved in any communication, let alone to evaluate the degree of involvement of each State. Moreover, even were it technically possible to create records of the routings of all calls and to analyze them for the purpose of apportioning the charges and computing the tax on such of those calls, the time, equipment, and expense required would be staggering. As a result, MCI believes that such call-by-call apportionment would be utterly impracticable, if not truly impossible.

Fortunately, existing Commerce Clause jurisprudence accommodates taxation of technologies for which apportionment, other than that inherent in careful definition of the tax base (e.g. limitation to in-state sales), cannot be practically achieved. The Court reiterated last year that unapportioned taxes "may be perfectly valid when administrative difficulties make collection of more finely calibrated user charges impracticable. . . ." *American Trucking Associations, Inc. v. Scheiner*, 107 S. Ct. 2829, 2847 (1987).

This principle is illustrated by *Capitol Greyhound Lines v. Brice*, 339 U.S. 542 (1950), where the Court upheld a 2% tax on the fair market value of motor vehicles for the use of State highways. In that case, it was argued "that a tax on vehicle value should be forbidden. . .because it varies for each carrier without relation to road use." 339 U.S. at 545. The Court upheld the tax under the Commerce Clause, recognizing that "[c]omplete fairness would require that a state tax formula vary with every factor affecting appropriate compensation for road use" and that "we must be content with 'rough approximation rather than precision.'" 339 U.S. at 545, 546.

Similarly, in *Aero Mayflower Transit Co. v. Board of R.R. Commissioners*, 332 U.S. 495 (1947), the Court upheld State power to assess a $15 minimum fee on each vehicle operated by a motor carrier on the State's highways. It reasoned that the Constitution did not "require the state to elaborate a system of motor vehicle taxation which will reflect with exact precision every gradation in use." *Id.* at 506 n.19. The Court has explained this decision as "based on the costs the State would encounter in collecting taxes for vehicles that earned less than $3,000 annually in Montana. We also emphasized the administrative impossibility of precise apportionment according to road use in *Capital Greyhound Lines v. Brice*." *Scheiner*, 107 S. Ct. at 2847 n.26.

To be sure, *Scheiner* held that flat fees and taxes for use of a State's roads were no longer permissible because "[t]he administrative machinery of revenue collection for highways is now obviously capable of taking into account at least the gross variations in cost per unit of highway usage. . . ." *Id.* at 2847. Nonetheless, the Court emphasized that *Capitol Greyhound Lines*, *Aero Mayflower Transit*, and similar cases remain valid precedents for "their recognition that the Commerce Clause does not require the States to avoid flat taxes when they are the only practicable means of collecting revenues from users and the use of a more finely gradated user fee schedule would pose genuine administrative burdens." *Id.* (footnote omitted).

In sum, the Court has repeatedly "recognized that [administrative]. . .burdens may be sufficient to justify states in ignoring even . . . key factor[s]" that might be included in an analytically perfect apportionment. *Evansville-Vanderburgh Airport Authority District v. Delta Airlines*, 405 U.S. 707, 716 (1972). That principle should be applied here, where apportionment of the tax on each individual call is obviously impracticable[12] and the method for allocating calls to Illinois for tax purposes is itself a proper method of apportioning the tax base among the States.

Appellants rely (Goldberg Br. 18, 21, 34; GTE Sprint Br. 10-12, 22,24 25, 30) heavily on *Central Greyhound Lines, Inc. v. Mealey*, 334 U.S. 653 (1948), in support of their contention that each call taxed must be apportioned to the portion of the transmission occurring within Illinois. In *Mealey*, the Court forbade New York to tax the entire gross receipts of a bus company for transporting passengers between points in New York over routes that lay largely in Pennsylvania and New Jersey. However, the Court reached that result only after noting that "[t]here is no dispute as to feasibility in apportioning this tax." *Id.* at 663, 662

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[12] The summary judgment record below did not address the feasibility of apportionment of individual telephone calls. However, the challenger of the constitutionality of a tax bears the burden of clearly and cogently demonstrating all facts necessary to establish its invalidity. *Norton Co. v. Department of Revenue*, 340 U.S. 534, 537 (1951); *Container Corp. of America v. Franchise Tax Board*, 463 U.S. 159, 175-76 (1983). Thus, appellants were obliged to prove that apportionment is practicable before they could demand that one be made.

(proportion of mileage traveled in New York known to four decimal places). Moreover, the extent of the use made of the roads of one State by a given bus in this continuous transportation was, of necessity, almost exactly proportional to the mileage in that State, for the nature of the use was virtually identical.

Here, in contrast, the feasibility of apportionment is very much in dispute and there has been no showing of such feasibility. Not only are the paths of individual communications practically undeterminable, but even such determination would not eliminate the need to evaluate the disparate impacts of the wide variety of different transmission methods utilized in the respective States through which those communications pass. Under these circumstances, the applicable rule is that for situations where more precise apportionment is impracticable.

B. Illinois Has Taxed No More Than Its Fair Share of the Interstate Telecommunications Activity Connected to the State.

Moreover, even were it barely within the realm of practicality to make some more precise apportionment of individual calls, requiring such an apportionment would simply create substantial burdens which would serve no purpose in more fairly dividing the interstate tax base among the States or facilitating interstate commerce. A crude example would be for a State to tax 50% of the charges for each interstate call originating or terminating in that State, regardless of the location to which it is charged. Such a charge would be more complicated to administer than the Illinois tax, but there is no reason to believe that it would produce a significantly different distribution of revenue, for it is unlikely that the percentages of such calls charged to telephones in a given State is much different from the percentage charged to telephones elsewhere.

A more sophisticated apportionment would have each State tax its "proportionate share" (assuming that this proportion could even be determined) of every call originating or terminating in that State or transmitted in part through that State. Such an apportionment would presumably favor States, like Illinois,

which are centrally located and participate in the transmission of many calls between other States on either side. It should be obvious that any such tax would be an administrative nightmare. Moreover, even apart from the enormous costs of administration of such tax schemes, its adoption by Illinois would likely create a *greater* burden on interstate commerce than the present Illinois tax because of the tax which would be imposed on the great volume of calls (now untaxed by Illinois) transiting Illinois en route between other States.

In short, the Illinois tax reaches no more than a fair share of the total interstate telecommunications activity involving Illinois and uses the least costly and most practicable method of allocating a fair portion of that activity to itself. Especially in the absence of any showing that a more precise method of apportionment is practicable, the Illinois tax should be recognized as a proper application of the principle that "[i]t was not the purpose of the commerce clause to relieve those engaged in interstate commerce from their just share of state tax burden. . . ." *Western Live Stock v. Bureau of Revenue*, 303 U.S. 250, 254 (1938). Because Illinois has demanded no more than its "just share," the challenged tax should be upheld against appellants' claims of inadequate apportionment.

III. THE ILLINOIS TAX CREATES NO IMPERMISSIBLE RISK OF MULTIPLE TAXATION

A. The Illinois Tax Is Internally Consistent and Many of the Alleged Risks of Multiple Taxation Result from Other Taxes Which Are Not Internally Consistent.

Appellants argue that the Illinois tax violates the Commerce Clause by creating a "risk of multiple taxation," as evidenced by its failing the test of "internal consistency." (GTE Sprint Br. 26-29). That test requires that "the formula [by which the tax is applied] must be such that, if applied by every jurisdiction, it would result in no more than all of the [charge on a single telecommunication] being taxed." *Container Corp. of America v. Franchise Tax Board*, 463 U.S. 159, 170 (1983).

The Illinois tax satisfies the internal consistency test, because if every jurisdiction adopted a telecommunication excise tax imposed on charges to the consumer's service address, each telecommunication would be taxed exactly once. Indeed, GTE Sprint, at least, concedes that "if every state passed a tax *identical* to the Illinois tax, it is true only one state would tax a long distance call. . . ." (GTE Sprint Br. 27.)

Appellants argue that there is nonetheless an impermissible risk of multiple taxation resulting from the coexistence of the Illinois tax with actual or hypothetical taxes that they characterize as similar to the Illinois tax. GTE Sprint, at least, contends that these taxes must be regarded as "like" taxes for purposes of the internal consistency test and that, if they are so regarded, the Illinois tax fails that test. (GTE Sprint Br. 26-29.) However, this contention reflects a fundamental misunderstanding of the rule laid down by the Court to balance Commerce Clause concerns against the need to allow for a wide variety of local tax structures. Moreover, many of the risks of multiple taxation on which appellants rely result, not from any defect in the Illinois tax, but rather from the failure of the (actual or hypothetical) other tax to satisfy the internal consistency requirement.

The Court has not applied the internal consistency requirement by seeking to define some class of "similar" taxes whose interactions with the tax in question must be considered. Rather, it has focused solely on the effects which would follow if other States adopted "the precise [tax] scheme" at issue. *Armco Inc. v. Hardesty*, 467 U.S. 638, 644 (1984). While Justice (now Chief Justice) Rehnquist opposed the imposition of this requirement, he too understood it to address only "the impact on interstate commerce if other jurisdictions employed *the same tax*." *Id.* at 648 (dissenting opinion) (emphasis added). *See also Tyler Pipe Industries, Inc. v. Washington State Department of Revenue*, 107 S. Ct. 2810, 2816-20 (1987); *Id.* at 2826 (dissenting opinion); *American Trucking Associations, Inc. v. Scheiner*, 107 S. Ct. 2829, 2840 (1987); *Id.* at 2851 (dissenting opinion). Indeed, it is precisely the fact that the rule depends solely on the form of

the tax under consideration that it can be described as one of *internal* consistency. There no claim that the Illinois tax fails this test.

Rather, GTE Sprint argues that a broader analysis is necessary in order to prevent "other states which host and economically support significant transmission, billing, and purchase activity on [the same] call [from being] deprived of revenues based on those activities." (GTE Sprint Br. 27.) However, as shown at 20-21, *supra*, Illinois has not attempted to appropriate more than its fair share of the telecommunications activities which it "host[s] and economically support[s]," so that other States are left free to tax their own shares of the overall activity without subjecting interstate commerce to any undue or discriminatory burden.[13]

The lack of any need for a broader restriction is underscored by the efficacy of even the narrow restriction to prevent the sorts of multiple taxation that appellants purport to fear. Upon examination, many of those risks stem from the lack of internal consistency of the other taxes allegedly creating the multiple burden rather than from any defect in the Illinois tax.

[13] Moreover, it would be an undue intrusion on State taxing power to adopt the sort of ill-defined broadening of the internal consistency rule advocated by GTE Sprint. As argued by the dissents in *Armco*, *Tyler Pipe*, and *Scheiner*, the propriety of the internal consistency rule itself was not entirely free from doubt. Presumably, the Court found those doubts outweighed by the rule's simplicity and ease of administration as well as by the severity of the risks of multiple taxation posed by internally inconsistent taxes.

However, extension of the rule to some ill-defined class of "similar" taxes will destroy both its simplicity (by requiring determination of what taxes must by considered similar) and its limitation to particularly severe risks of multiple taxation (because the broadening of the test will necessarily reach a broader class of risks). Since such broadening is unnecessary to protect either the freedom of interstate commerce or the taxing interests of other States, it would be improper to further constrain the permissible structures of State taxation.

One way in which a tax structure may lack internal consistency is to impose a single tax on multiple aspects of the same transaction, despite the fact that those aspects might occur in different States. Thus, in *Tyler Pipe*, the tax covered both manufacturing and sale in the taxing State, so that a given transaction would be subject to only one tax if both activities occurred in the same States but would be subject to two equivalent taxes if those activities occurred in different States. Many of the non-Illinois taxes relied upon by appellants have this defect.

For example, GTE Sprint discusses a hypothetical New York tax and an actual Washington tax which apply to all interstate calls originating or terminating in the taxing State and either Abilled or paid there (GTE Sprint Br. 35-36.) As GTE Sprint notes, "a call [between Illinois and New York] might be *charged* to a phone at the Illinois division of a New York corporation, but the bill *paid* at corporate headquarters in New York," resulting in double taxation of the same call. (GTE Sprint Br. 35 n. 14)(emphasis in original). The problem arises from the internal inconsistency of the hypothetical New York tax. If that tax were in effect in both Illinois and New York, and the call used in the example were billed to the Illinois division and paid in New York, the multiple taxation would occur because a single tax has been imposed on multiple aspects (here, billing and payment) of the same transaction. Thus, it is the hypothetical New York tax which is internally inconsistent. This problem occurs wherever a state utilizes multiple events, several of which may occur in a single transaction and in different States, to trigger the application of the tax.

The Illinois tax does not suffer from this problem, for any given charge can be made only to a single service address. Thus, under the Illinois scheme, such a charge can be subjected to only one tax. Obviously, where any multiple taxation results from the imposition by another State of an unconstitutional tax, that should not impair the validity of the internally consistent and otherwise proper Illinois tax.

B. Any Risk of Multiple Taxation Which Might Result from the Illinois Tax Is No Different from the Unavoidable Risks Which Result from All Variations in State Apportionment Schemes.

Even if another State's tax avoids the pitfall of internal inconsistency, it is still possible that some calls taxed by Illinois might also be subjected to taxation by another jurisdiction which taxes an appropriate share of the interstate telecommunications activity affecting it but arrives at that share in a different manner. The most obvious way (and the most significant one illustrated by any of the actual taxes cited by appellants) would be for a State to tax calls on the basis of where they are billed instead of the location of the service address where they are charged.

Apart from the possibility of a credit against one tax or the other, see discussion at 29, *infra*, there are two ways of disposing of this problem. First, it is arguable that use of the billing address (rather than the service address) is itself improper. Second, and more fundamentally, any multiple taxation resulting from this sort of an overlap does not result from any discrimination against interstate commerce, but is the sort of inevitable result of varying State apportionment mechanisms which the Court has previously held permissible. *Moorman Manufacturing Co. v. Bair*, 467 U.S. 267, 278 (1978).

The questionable propriety of using the billing address as the basis of taxation results from the requirement that a tax on interstate commerce be "fairly related to the services provided by the State." *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977); *Commonwealth Edison Co. v. Montana*, 453 U.S. 609, 620-30 (1981). As the Court explained in *Commonwealth Edison*, "there is no requirement . . . that the amount of general revenue taxes collected from a particular activity must be reasonably related to the value of the services provided to the activity." *Id.* at 622. Rather, "'[t]he only benefit to which the taxpayer is constitutionally entitled is that derived from his enjoyment of the privileges of living in an organized society, established and safeguarded by the devotion of taxes to public purposes.' "

Id. at 623, quoting *Carmichael v. Southern Coal & Coke Co.*, 301 U.S. 495, 521-23 (1937). Thus, the requirement of a fair relationship to the benefits provided by the State requires that "the *measure* of the tax must be reasonably related to the extent of the contacts. . ." between the State and the activity of the taxpayer on which the tax is imposed. 453 U.S. at 626.

Measuring a tax by the purchase price of the telecommunications charged to a service address within the taxing State clearly satisfies the requirement of fair relationship to services, for the measure is based on the taxpayer's use of the telephone(s) located at that address and thereby relates to the value of such services as the police and fire protection afforded to that service address and the telephone(s) located there.[14] *See D.H. Holmes Co. v. McNamara*, 56 U.S.L.W. 4400, 4402 (1988) (Tax on distribution of catalog to in-state customers upheld on basis of relationship to protections afforded to taxpayer's in-state stores).

[14] A fundamental error running throughout appellants' argument is the persistent claim that the tax is invalid unless proportioned to the protections which Illinois provides to the interstate telephone network, completely ignoring the role of the tax as a measure of the protections provided to the taxpayer at the Illinois service address. That error leads to the mistaken claim that, like the flat tax for road use in *American Trucking Associations, Inc. v. Scheiner*, the Illinois tax bears more heavily on interstate commerce (for which only a portion of the transmission occurs in Illinois) than on intrastate commerce (where the entire transmission occurs in Illinois). However, the vice of the tax in *Scheiner* was its tendency to place a disproportionate burden on out-of-state truckers, who (the evidence showed) had far less occasion to utilize the privileges for which the flat fee was levied. Thus, the tax in *Scheiner* discriminated in the sense that it "favor[ed] in-state business over out-of-state business for no other reason than the location of its business." 107 S. Ct. at 2841. There is no evidence tending to show that the Illinois telecommunications tax has any similar tendency. To the contrary, the analysis set forth in this brief shows that the Illinois tax is designed in a manner which places the entire burden on taxpayers with Illinois service addresses in proportion to their respective Illinois activities, so that there is no danger of shifting the tax burden to out-of-state interests.

On the other hand, if a taxpayer were to elect to pay all its bills from a centralized location, the bills paid necessarily reflect all of its activities throughout the nation, and would not appear to constitute a fair measure of the services provided by the taxing State. Use of the billing address would also allocate an unfair share of the tax base to States with concentrations of corporate headquarters offices rather than to the States where the corporate operations and telephones are located. Thus, use of the billing address as the basis of taxation appears significantly less proper than use of the service address.[15]

More fundamentally, the overlap in taxation arising from variations among State tax schemes is inevitable whenever different States use different apportionment mechanisms. If all of the apportionment mechanisms are individually fair, then the variations will largely cancel one another out. Thus, if another State bases taxation on the billing address and Illinois bases it on the services address, then calls billed to the other State but charged to an Illinois service address will be taxed twice. However, if the billing and service addresses are reversed, there would be no tax at all. While particular transactions might suffer multiple taxation, interstate commerce as a whole would pay no more than its fair share and would suffer no undue burden.

This analysis is part of the basis of the Court's express holding in *Moorman Manufacturing Co. v. Bair*, 437 U.S. 267 (1978), that the risk of multiple taxation arising out of differences among

[15] To be sure, by use of credit cards, calls may be charged to a service address even though none of the phones at that address are involved in those calls. Nonetheless, use of the telephone even as a basis for billing is a measure of the utility of that phone to the purchaser. This will be especially true if the purchaser has no other phones to which the call might have been charged or if charging calls to the particular phone assists in allocating them to particular customers or operations. Moreover, because credit card calls are generally more expensive than direct dialed calls, purchasers are unlikely to use credit cards unless making calls from phones other than their own. In contrast, there are no significant costs associated with directing bills to a location different from the service address.

State apportionment schemes does not render a state tax invalid under the Commerce Clause. *Moorman* upheld the validity of the Iowa single-factor formula employed to apportion income of interstate businesses for income tax purposes, even though forty-four of the forty-five States other than Iowa imposing such a tax utilized a different apportionment formula, and the differences resulted in some duplication of Iowa's taxation.

The Court explained that such duplication does not amount to constitutionally impermissible multiple taxation:

> The only conceivable constitutional basis for invalidating the Iowa statute would be that the Commerce Clause prohibits any overlap in the computation of taxable income by the States. If the Constitution were read to mandate such precision in interstate taxation, the consequences would extend far beyond this particular case. For some risk of duplicative taxation exists whenever the States in which a corporation does business do not follow identical rules for the division of income . . . .
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> The prevention of duplicative taxation, therefore, would require national uniform rules for the division of income. Although the adoption of a uniform code would undeniably advance the policies that underlie the Commerce Clause, it would require a policy decision based on political and economic considerations that vary from State to State. The Constitution, however, is neutral with respect to the content of any uniform rule . . . .
>
> While the freedom of the States to formulate independent policy in this area may have to yield to an overriding national interest in uniformity, the content of any uniform rules to which they must subscribe should be determined only after due consideration is given to the interests of all affected States. It is clear that the legislative power granted to Congress by the Commerce Clause of the Constitution would amply justify the enactment of legislation requiring all States to adhere to uniform rules for the division of income. It is to that body, and not this Court, that the Constitution has committed such policy decisions.

Id. at 278-80.

So too here, particularly since no apportionment scheme allegedly superior to that utilized by Illinois has been shown to be feasible, the Court should not strike down the Illinois tax.

C. Illinois Has Provided Additional Protection Against Actual Multistate Taxation By Offering a Credit for Taxes Paid to Any Other State on a Call Taxed by Illinois.

For the reasons set forth above, limitation of the tax base to interstate calls both originating and terminating in Illinois and charged to an Illinois service address provides adequate protection against any undue burden on interstate commerce. However, Illinois has taken the further step of granting a credit against the tax previously paid to Illinois to any taxpayer who pays taxes in both Illinois and another State on the same call.[16] Act § 4. The credit is equal to the full "amount of such tax properly due and paid in such other state." *Id.*

Appellants object to this credit as a protection against actual multiple taxation because it cannot, except by accident, fairly divide the revenues from a given call among the States involved in transmission of that call. (Goldberg Br. 26; GTE Sprint Br. 15, 41-42.) This is true, but irrelevant, for call-by-call apportionment is not constitutionally required.

Appellants also complain that the standards for granting the credit are ill-defined and the procedures necessary to claim it are unduly burdensome. (Goldberg Br. 4, 26-27; GTE Sprint Br.

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[16] It is true that this credit would not protect against imposition of taxes by multiple States on different taxpayers. (Goldberg Br. 11, 23.) However, the tax is laid on the amount paid by the purchaser of the call, and there is almost never more than one purchaser paying a given charge. Consequently, this risk seems remote, at best. Moreover, if this situation does somehow arise and each of the other taxes involved is fairly apportioned, there would be no undue burden on commerce for the reasons explained at 25-29, *supra*.

15-16, 42-44.) However, as the State of Illinois correctly pointed out (Consolidated Mo. to Affirm 13 n.5), the alleged inadequacies of the credit mechanism cannot properly be evaluated on this record, which neither shows any actual instance of multiple taxation nor any actual attempt to invoke that procedure.

CONCLUSION

For the reasons stated, the judgment of the Illinois Supreme Court should be affirmed.

Respectfully submitted,

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